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SUPPLEMENT
TO
FEDERAL INCOME TAX

**INCLUDING TAX ON UNDISTRIBUTED NET
INCOME, CAPITAL STOCK TAX,
WAR EXCESS PROFITS TAX
AND
STAMP TAX**

BY
GEORGE E. HOLMES
of the New York Bar

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PREFACE

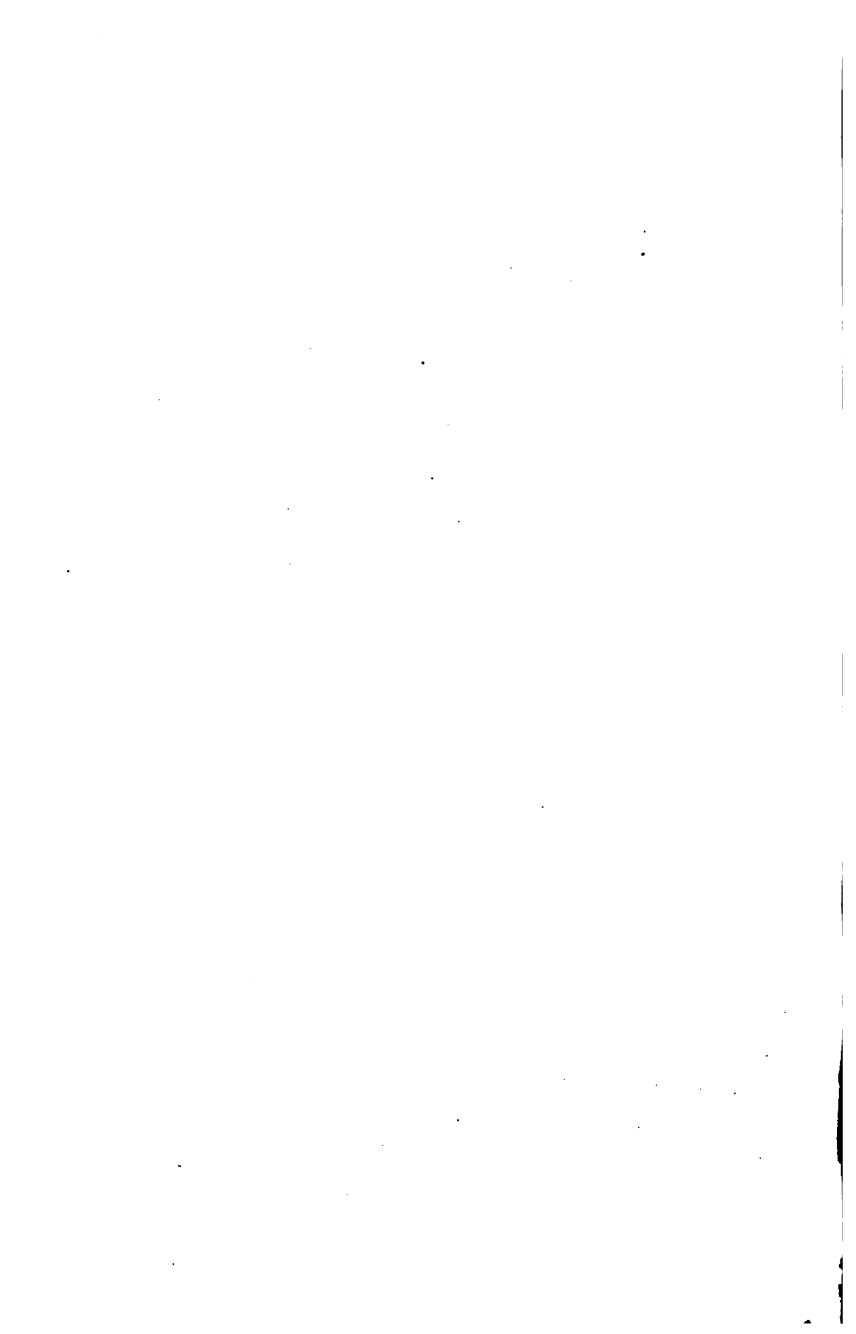
Since the publication of the first edition of *Holmes Income Tax*, the Treasury Department has issued a new compilation of rulings, known as Regulation 33, Revised. Several Treasury decisions have also been published amending or repealing former rulings or announcing the construction of the Treasury Department on points which were unsettled at the time of publishing the first edition. The recent rulings and regulations are set forth in this supplement, reference being made to the pages in *Holmes Income Tax* where may be found statements on the same subjects.

The Treasury Department has also issued a compilation of rulings on the War Excess Profits Tax, which are printed in full herein, together with notes and cross-references by the author.

A new chapter has been added, dealing with the Stamp Taxes.

The Author's thanks are again extended to The Corporation Trust Company of New York City for the use of its valuable Income Tax Service and War Tax Service in the preparation of this new matter. Their War Tax Service for 1914 and 1915 was of particular value as a source of information regarding the rulings under the Stamp Tax Law of October 22, 1914.

GEORGE E. HOLMES.



SUPPLEMENT TO HOLMES INCOME TAX

CHAPTER 1

INTRODUCTION

[Page 5.]

Retroactive Effect of Rulings. Treasury Department decisions promulgating rulings of the Internal Revenue Bureau become effective upon the date of approval unless otherwise stated therein. Cases previously adjusted in contravention of law as pronounced in such decisions, are subject to readjustment in accordance with the decision. (Reg. 33 Rev., Art. 38.)

[Page 9.]

Record to be Kept. Every individual, partnership, corporation, or association liable to any tax imposed under the internal revenue laws of the United States or for the collection thereof shall keep such records and render such statements and return, under oath, as shall be prescribed by the Commissioner of Internal Revenue. (Reg. 33 Rev., Art. 50.)

CHAPTER 3

INDIVIDUALS TO WHOM THE LAW IS APPLICABLE

[Page 25.]

Minors. For income tax purposes majority is attained at 21, unless the statute of the state of residence

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otherwise provides. (Telegram from Treasury Department dated January 25, 1918; I. T. S., 1918, Par. 3074.) The parent is held to be the natural guardian of a minor child. Income received by the minor child from sources other than the parent should be included by the parent in his return of income. The fact that such income is not appropriated by the parent is immaterial, as it will be held, in the absence of a showing of fact to the contrary, that such income was subject to appropriation and was appropriated by the parent, and that the child receives the same as a gift from the parent. Where the income is from a separate estate and the parent has been appointed guardian and the conditions are such that the income so received is to be held for the use of the child, it shall not be included in the return of income of the parent, but shall be accounted for otherwise for the purpose of the income tax in manner and form as called for by the facts of the particular case. (Reg. 33 Rev., Art. 29.)

CHAPTER 4

CITIZENS AND RESIDENTS OF THE UNITED STATES

[Page 33.]

Losses Not Incurred in Trade. The next to the last sentence of the paragraph (on page 34) should read as follows: "He is thus required to pay a tax on only the net gain from such transactions during the year."

[Page 36.]

Contributions to Charities. In connection with claim for this deduction on returns of income there shall be stated:

(a) The name and address of each organization to which a gift was made.

(b) The date and amount of the gift in each case.

Where the gift is other than money, the basis for calculation of the value of the gift shall be the fair market value of the property the subject of gift at the time of the gift. (Reg. 33 Rev., Art. 8.)

CHAPTER 5

NON-RESIDENT ALIENS

[Page 48.]

Salaries Paid by Resident Employers. It is held that salaries, wages, commissions, and rents paid by domestic corporations resident individuals, or partnerships to non-resident alien employees for services rendered entirely in a foreign country and for property located in a foreign country are not subject to deduction and withholding of the normal tax, and such payments of income will not be subject to the income tax in the hands of the recipient as from a source within the United States. (Reg. 33 Rev., Art. 32.)

[Page 50.]

Profits on the Sale of Property. When a non-resident alien who owns stock in an American corporation disposes of same by sale, the sale and delivery being made within the United States, the profit will be held to have been derived from sources within the United States and is to be included for the purpose of income tax. (Reg. 33 Rev., Art. 4.)

[Page 55.]

Return of Annual Net Income. A non-resident alien individual shall make a full and accurate return of all net income received from sources within the United States, regardless of amount unless the tax on such income has been fully paid at the source; and is not entitled to the benefit of the several deductions and credits provided by section 6 of the act of September 8, 1916, as amended by the act of October 3, 1917, unless such return is filed by him or his authorized agent. (Reg. 33 Rev., Art. 32.)

[Page 55, Note 43.]

When all income tax to which income of a non-resident alien is subject is not withheld at the source, a return of income will be required to be filed by or on behalf of said non-resident alien, and penalty for failure to make return in time will attach. All property in the United States of a non-resident alien will be subject to distraint for collection of tax and penalty. (Reg. 33 Rev., Art. 13.)

[Page 58.]

Abatement and Refund. Where, upon filing return of income, it appears that a non-resident alien is not liable for income tax, but, nevertheless, income tax shall have been withheld at the source, in order to obtain a refund on the basis of the showing made by the return there shall be attached to the return a statement showing accurately the amounts of tax withheld, with the names and post offices addresses of all withholding agents. (Reg. 33 Rev., Art. 32.)

CHAPTER 6

RESIDENT AGENTS FOR NON-RESIDENT ALIENS, FOREIGN CORPORATIONS AND FOREIGN PARTNERSHIPS

[Page 62.]

Duties and Liabilities of Resident Agents. The responsible heads or representatives of non-resident aliens in connection with any sources which said non-resident aliens may have within the United States, shall make a full and complete return of such income and shall pay any and all tax, normal and additional, assessed upon the income received by them in behalf of their non-resident alien principals, in all cases where the income tax on income so in their receipt, custody, or control shall not have been withheld at the source.

Where non-resident aliens have various sources of income within the United States so that at any one source or from all sources combined, the amount of income shall call for the assessment of additional tax and a return of income shall not be filed by or on behalf of a non-resident alien for the purpose of the assessment of income tax, the Commissioner of Internal Revenue will cause a return of income to be made and include therein the income of the non-resident alien from all sources concerning which he has information and shall assess the tax and collect the same from one or more or all of the sources of income within the United States of said non-resident alien, without allowance for deductions and credits under section 6. (Reg. 33 Rev., Art. 32.)

[Page 63.]

Making Returns for Non-Resident Principal. The agent of a non-resident alien is responsible for a correct

return of all income accruing to his principal within the purview of the agency, and the agent will be held responsible for a complete return of all such income. The agency appointment will determine how completely the agent is substituted for the principal for income tax purposes. (Reg. 33 Rev., Art. 32.)

[Page 64.]

Paying the Tax for Non-Resident Principal. Income derived by non-resident aliens from sources in the United States is subject to the normal or additional tax, or both, as the case may be, and said tax shall be paid by the owner of said income, or the proper representative of the non-resident alien having the receipt, custody, control, or disposal of the same. In all cases the proper representative in the United States of a non-resident alien, with respect to such income, shall make return for such non-resident of all such income coming into his custody or control and pay the tax thereon as provided by law; provided, however, where all income shall have been paid over by the representative to his principal on or before October 3, 1917, under the law and income tax regulations in force up to that date, or where the stockholder or record shall not—between October 3 and December 31, 1917,—be in receipt of or have in his custody or control income the property of his said principal, such representative will be relieved from paying said tax, leaving the same a charge against the non-resident alien and to be collected from him by any means at the disposal of the Commissioner of Internal Revenue; but where such representative shall have in his possession, custody, or control subsequent to October 3, 1917, income of such non-resident alien, said representative shall pay the

total tax due upon the income of such non-resident alien so in his custody and control for the entire year 1917 and subsequent years. (Reg. 33 Rev., Art. 32.)

CHAPTER 7

NOMINAL STOCKHOLDERS

[Page 68.]

Procedure When Actual Owner Is Non-Resident. In all cases where the actual owner is a non-resident alien, individual or corporation, and the record owner is an individual, firm, or corporation in the United States (a citizen or resident alien), and the aforesaid showing of actual ownership is made, the record owner will be held, for income-tax purposes, to have the receipt, custody, control, and disposal of the dividend income and will be required to make return for the actual owner and pay the tax found by such return to be due. Where the actual owner is a non-resident alien corporation, return will be made regardless of the amount of dividend and the normal income tax will be paid, and when the actual owner is a non-resident alien individual, a return shall be made regardless of the amount of the income, and when the net amount of such income exceeds \$5,000 said custodian shall also pay the additional tax on such income. When it shall appear from the disclosure herein provided for that the actual owner is a non-resident alien partnership, all certificates making such disclosure shall be transferred to the Commissioner of Internal Revenue for the information of the collector of internal revenue, but no return will be made for such partnership and no amount will be retained from such income by the representative of such partnership in the United States unless and until such

representative shall be so instructed by the Commissioner of Internal Revenue. (Reg. 33 Rev., Art. 32.)

In all cases where the actual owner of stock is a non-resident alien corporation and the record owner is an individual, firm, or corporation in the United States, citizen, or resident alien, and the actual ownership has been disclosed, the record owner will be held for income tax purposes to have the receipt, custody, control, and disposal of the dividend and will be required to make return for the actual owner and pay the tax found by such return to be due. (Reg. 33 Rev., Art. 201.)

The record owner is held to be "the proper representative having the receipt, custody, control, or disposal" of income of the actual owner and is required to file a return for or on behalf of the actual owner for the purpose of assessment of income tax not withheld at the source.

When a return is not required to be filed by or on behalf of the actual owner, the showing may be made upon the certification of the record owner.

Upon the showing thus made, either by certification or return, as the circumstances may require, the Commissioner of Internal Revenue will make such assessments and issue such instructions to debtors and withholding agents as will insure the proper collection of tax in accordance with the respective tax liabilities. (Reg. 33 Rev., Art. 32.)

[Page 69.]

Procedure When Nominal Stockholder Is a Non-Resident Alien. When the record owner of such stock is a non-resident alien corporation, etc., not having an office or place of business in the United States, the debtor corporation will withhold the normal income tax and

pay the same to the proper officer of the United States authorized to receive it in manner and form provided for withholding and accounting for tax withheld.

When a non-resident alien record owner of stock of domestic or resident corporations is an organization subject to withholding at the source of dividend payments, but is not the actual owner of the stock, such record owner may make disclosure, in form prescribed by the Commissioner of Internal Revenue, of actual ownership, in which case said domestic or resident corporations will be governed by the established facts.

If the record owner does not exercise his right to disclose actual ownership for the purpose of claiming exemption from having tax withheld at the source, debtor corporations and their withholding agents in the United States will be held liable on their stock records of ownership for the tax required to be withheld by section 13 (f) of the act of September 8, 1916.

In the absence of disclosure of actual ownership filed with debtor corporations or their withholding agents, in manner and form provided for, the normal tax required to be withheld in accordance with stock records of ownership can only be released to a record owner not liable for tax upon a proper showing to the Commissioner of Internal Revenue of record and actual ownership, the names and post office addresses of debtor corporations and withholding agents, and the amounts withheld. (Reg. 33 Rev., Art. 32.)

CHAPTER 8

FIDUCIARIES

[Page 74.]

Who Are Fiduciaries. "Fiduciary" is a term which applies to all persons or corporations that occupy posi-

tions of peculiar confidence toward others, such as trustees, executors, or administrators; and the fiduciary for income tax purposes is any person or corporation that holds in trust an estate of another person. (Reg. 33 Rev., Art. 29.)

[Page 77.]

Duties of Executors and Administrators. If the net income of a decedent from January 1 to the date of his death within that year was \$1,000 or over, if unmarried, or \$2,000 or over if married, a return for such decedent must be made by the executor or administrator, and such executor or administrator may claim all deductions and exemptions to which the decedent would have been entitled under the law. (Reg. 33 Rev., Art. 4.)

Liability for payment of income tax *attaches to the person* of an *executor or administrator* for income tax up to and including the date of his discharge, regardless of the fact that the time in which claim is made and filed against the estate has expired or where, prior to distribution and discharge, the executor or administrator had notice of his obligations to the Federal Government or where he failed to exercise due diligence in determining whether or not such obligations existed.

Liability for the tax due from a deceased person, or from his estate, also attaches to the estate itself, and when by reason of distribution of the estate and discharge of the executor or administrator it shall appear that collection of the tax cannot be made from the executor or administrator, the collector will make demand on the distributees for their proportionate share of the tax due and unpaid. (Reg. 33 Rev., Art. 29.)

[Page 78.]

Receiver. Receivers who, as officers of a court, stand in the stead of some principal are required to account for income tax as the principal would have been required to account. (Reg. 33 Rev., Art. 26.)

[Page 79.]

Trust Estates. A deed of trust must be absolute so far as the conveyance of title is concerned and irrevocable by the donor, otherwise the income from the property in question will accrue to the donor and must be accounted for by him. (Reg. 33 Rev., Art. 29.)

[Page 79.]

Income of Trust Estates. Where, during the period of administration, an executor converts the estate in his possession as such executor into money for the purpose of settling the estate and closing the administration and in which conversion a profit is realized which with other income exceeds \$1,000, a return of income should be made by the executor covering the period of administration in which should be included all gains, profits and income of the estate during such period, and he should pay the tax found by such return to be due. The income of the estate being thus freed of income tax liability may thereafter be dealt with without further regard to income tax requirements.

Proceeds of life insurance policies payable to the estate of a decedent, when received by an executor or administrator, are, in the amount by which such proceeds exceed the premium or premiums paid by the decedent, income of the estate to be accounted for by the executor or administrator under the provisions of section 2 (b), act of September 8, 1916. (Reg. 33 Rev., Art. 29.)

[Page 82.]

Depreciation. In the case of a trust estate where the terms of the will or trust or the decree of a court of competent jurisdiction provides for keeping the corpus of the estate intact, and where physical property forming a part of the corpus of such estate has suffered depreciation through its employment in business a deduction from gross income for the purpose of caring for this depreciation, where the deduction is applied or held by the fiduciary for making good such depreciation, may be claimed by the fiduciary in his return of income. Fiduciaries should set forth in connection with their returns the provisions of law, trust, or decree requiring such depreciation deduction where any exists or when actual depreciation occurs, the amount thereof, and that the same has been or will be preserved and applied as such. All amounts paid by fiduciaries to beneficiaries of trust estates from the income of such trust estates, whether from reserves or otherwise, are held to be distributions of income and will be treated for income tax purposes in accordance with the provisions of law and regulations applicable to income of such beneficiaries. (Reg. 33 Rev., Art. 29.)

[Page 86.]

Income Received During Settlement of Decedent's Estate. Under the provisions of section 2 (b) it is held that estates during the period of administration have but one beneficiary, and that beneficiary is the estate. Therefore a return on Form 1040 or 1040 A, subject to all the deductions and exemption, shall be made by the executor or administrator for such beneficiary and the entire tax paid thereon. (Reg. 33 Rev., Art. 29.)

[Page 87.]**Procedure in Reporting Undistributed Income.**

Where income under the provisions of section 2 (b), act of September 8, 1916, is accounted for in a return of income by the executor, administrator, or trustee, as the case may be, and the tax shall have been assessed and paid under such return, such income is thereby freed of all tax liability and may be thereafter dealt with without further regard to the provisions of the income tax law. (Reg. 33 Rev., Art. 29.)

[Page 91.]

When a Return Is Required. Fiduciaries are required to make returns of income on Income Tax Form 1041 whenever the interest of any beneficiary in the net income of an estate or trust for which the fiduciary acts is \$1,000 or over for an unmarried beneficiary, and in case there are married beneficiaries, then a return will be required whenever the interest of any such married beneficiary is \$2,000 or over. (Reg. 33 Rev., Art. 27.)

Administrators or executors may, immediately after their discharge, upon final accounting, file with the proper collector of internal revenue a return of income for the income of the estate for the calendar year in which the administration was closed, and should pay the tax found by such return to be due immediately upon receipt of notice and demand for the amount of such tax. There should be attached to this return a copy of the certificate, under seal, setting forth the fact of final accounting and discharge of the executor or administrator. The liability for return is fixed by the law as of December 31, and return will be required in

accordance with the provisions of law existing on that date.

An ancillary administrator is held to be merely an agent of the domiciliary administrator and should transmit to him all information as to income of the estate received by the ancillary administrator, to the end that the original administrator may make a return covering the entire income of the estate. (Reg. 33 Rev., Art. 26.)

[Page 95.]

Income to Be Reported by Beneficiary. All amounts paid by fiduciaries to beneficiaries of trust estates from the income of such trust estates, whether from reserves or otherwise, are held to be distributions of income and will be treated for income tax purposes in accordance with the provisions of law and regulations applicable to income of such beneficiaries. The beneficiary will be required in the case of trust estates to account for the actual amounts distributed or credited to him. (Reg. 33 Rev., Art. 29.)

CHAPTER 10

PARTNERSHIPS

[Page 103.]

Limited Partnerships. Limited partnerships—that is, partnerships having one or more special partners who may share in the profits of the firm but whose liability for the debts of the company is limited to the amount of capital invested by such special partner or partners—are held to be associations within the meaning of this title, and as such are required to make re-

turns of annual net income and pay any tax thereby shown to be due. The income received by the members out of the earnings of such limited partnerships will be treated in their personal returns in the same manner as if it were dividends on the stock of corporations and will be subject to the additional or surtaxes in the hands of the recipient. (Reg. 33 Rev., Art. 62.)

[Page 113.]

Fiscal Year. Any partnership may at its option designate the last day of any month as the close of its fiscal year. In each case where the partnership's fiscal year differs from the calendar year it shall, not less than 30 days prior to March 1, give notice in writing to the collector of internal revenue of the district in which its principal place of business is located that the day it has thus designated is the closing day of its fiscal year. (Reg. 33 Rev., Art. 31.)

[Page 115.]

Net Losses of Partnership. Where the result of partnership operation is a net loss, the loss will be divisible between the partners in the same proportion as net income would have been divisible, and may be used by the individual partners in their returns of income. (Reg. 33 Rev., Art. 30.)

CHAPTER 12

CORPORATIONS

[Page 126.]

Definition. "Corporation" or "corporations," as used in these regulations, shall be construed to include

all corporations, joint-stock companies and associations, and all insurance companies coming within the terms of the law, as well as all business trusts organized or created for the purpose of engaging in *commercial or industrial enterprises*, the capital of which is evidenced by certificates or shares of interest issued or issuable to members on the basis of which profits are distributed or distributable. (Reg. 33 Rev., Art. 57.)

[Page 126.]

Joint-Stock Companies and Associations. The term "joint-stock companies" or "associations" shall include associations, common-law trusts, or organizations by whatever name known which carry on or do business in an organized capacity, whether created under and pursuant to State laws, trust agreements, declarations of trusts, or otherwise, the net income of which, if any, is distributed or distributable among the members or shareholders on the basis of the capital stock which each holds, or where there is no capital stock, on the basis of the proportionate share or capital which each has, or has invested, in the business or property of the organization, all of which joint-stock companies or associations shall in their organized capacity be subject to the tax imposed by this act, and shall make returns of annual net income accordingly. (Reg. 33 Rev., Art. 58.)

[Page 131.]

Liability for Tax After Dissolution. A corporation which was dissolved in 1917, prior to passage of the war revenue act of October 3, 1917, is subject to tax under the act of September 8, 1916, as amended, and also to the war income tax and the war excess profits

tax imposed by the act of October 3, 1917 (Brady et al. v. Anderson, 240 Fed., 665). A corporation so situated will make a return on revised form 1031, covering the period in 1917 during which it was in business prior to its dissolution. If it shall have previously made a return covering this period and shall have paid any excess profits tax under the act of March 3, 1917, it shall be entitled to credit for the amount of such tax so paid against any excess profits tax assessable against it under Title II of the act of October 3, 1917. (Reg. 33 Rev., Art. 61.)

[Page 135.]

Treasury Stock. Treasury stock, wherever and whenever that term is used in connection with the accounts of the corporation or for income tax purposes, will be held to mean stock which had been previously issued by the corporation and which had been repossessed by it through purchase or otherwise and then carried on its books as an asset. If such stock is resold at a price in excess of its cost upon repossession, such excess shall be returned as income for the year in which resold. If, for the purpose of enabling a corporation to secure working capital, or for any other purpose, the stockholders donate or return to the corporation to be resold by it certain shares of stock of the company previously issued to them, the sale of such stock will be considered a capital transaction, and the proceeds of such sale will be treated as capital and will not constitute income to the corporation. (Reg. 33 Rev., Arts. 98 and 99.)

[Page 136.]

Expenses Incurred in Sale of Capital Stock. Any and all expenses incidental to or connected with the

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selling of the capital stock (common or preferred) of a corporation for the purpose of raising capital to be by it invested in property or employed in the business for which the corporation is organized are not an "expense of operation and maintenance" within the meaning of this title, and such expense is not an allowable deduction from the gross income, for the reason that such an expense is incurred in a capital transaction; that is, the raising of capital to be invested or employed in the business.

Such expense, like the discount at which the shares of stock may be sold, has the effect only to reduce the available capital of the corporation and cannot be used to reduce the income from operations; that is to say, any expense incident to the bringing of capital into the company, whether it be a new or a going concern, cannot be recouped out of or charged against the operating income. It is a capital loss or expense properly chargeable against the proceeds of the sale of the stock and reduces the capital rather than the earnings of the company. (Reg. 33 Rev., Art. 145.)

[Page 142.]

Indebtedness Outstanding at the Close of the Year. From the amount of indebtedness to be reported as indebtedness outstanding at the close of the year must be eliminated all indebtedness incurred in the purchase of securities the income from which is not subject to the income tax. (Reg. 33 Rev., Art. 182.) Nor shall such amount include indebtedness which is not bearing interest.

[Page 143.]

Car Trust Certificates. Equipment or car trust certificates issued by or for railroad companies are a means

by which such companies secure cars or other equipment, or the money which with such equipment is purchased.

The equipment becomes at once an asset of the company and the trust certificates secured by such assets are obligations of the railroad companies, similar to corporate bonds, mortgages, and like obligations. The trustees in whose names legal title to the equipment stands, are not an association within the meaning of this title, and are therefore not a taxable entity, but they are, for the purpose of this title, a fiscal agent, paying off the obligations, both principal and interest, of the railroad companies with funds appropriated by such companies.

The railroad companies may include these trust certificates in the amount of their bonded or other indebtedness reported, under item 2 of the return Form 1031, and the interest paid thereon, with interest paid on other obligations will be deductible, the aggregate amount so deducted not to exceed the limit fixed by law. (Reg. 33 Rev., Art. 188.)

[Page 150.]

Lessee Corporations. A railroad company operating leased or purchased lines as an integral part of its line or system, and keeping no separate books of account as to such leased or purchased line, and the income from the operating of which cannot be segregated, shall include in its income all receipts derived therefrom, and if bonded or other indebtedness of the leased or purchased line has been assumed by the operating company, it may deduct from its gross income the interest paid on such indebtedness, provided the interest so paid plus the interest paid on its own indebtedness is

not in excess of the limit fixed by the law. In this event the leased or purchased line so long as it has a corporate existence will make return of annual net income setting out that on its own account it has neither income nor expenses, and that both are taken up in the return of the operating company, naming it. (Reg. 33 Rev., Art. 125.)

[Page 151.]

Lessor Corporations. If the leased or purchased line keeps separate books of account, or the income from its operations is, or can be segregated, or if the lessee or operating company pays it a certain rental, or in lieu of rental pays a certain per cent of dividends on its stock, interest on its bonds, taxes, etc., it (the lessor) will return the same as its income and will be subject to tax accordingly, and the lessee or operating company will make its return as though it were in no way related to the leased line. (Reg. 33 Rev., Art. 125.)

[Page 151.]

Stock Trust Certificates. Stock trust certificates or leased line certificates, as the case may be, issued by the lessee for the purpose of securing or holding control of the stock of the lessor are held to be issued in lieu of the certificates of capital stock, and for the purpose of this tax will be treated as capital stock and the amounts received by the holders of these certificates are dividends to the holders, to be treated as rentals by both lessee and lessor and constitute an allowable deduction in the one case and an item of income in the other, accordingly as they are paid and received. (Reg. 33 Rev., Art. 104.)

[Page 153.]

Fiscal Year. For the purpose of the 4 per cent additional tax imposed by the act of October 3, 1917, it is provided that in the case of a corporation making its return on the basis of its own fiscal year (other than the calendar year) this tax, for a fiscal year ending during the calendar year 1917, shall be levied, only on that proportion of its net income (less dividends received) which the period from January 1, 1917, to the end of the fiscal year bears to the entire fiscal year.

If the last previous return was made for the period ended December 31, 1916, and a return is made for a fiscal period ended with the last day of some month in 1917, the tax will be computed on the entire net income so returned. (Reg. 33 Rev., Art. 82.)

CHAPTER 13**SPECIAL PROVISIONS APPLYING TO INSURANCE COMPANIES****[Page 166.]**

Returns to Conform to State Reports. Returns of insurance companies must be rendered in conformity with reports made for the same period to the State insurance departments. As all insurance companies are required by law to render their reports to the various State insurance departments for the calendar year, their returns of annual net income for the purpose of the income tax should be made for the same period, unless their books are actually kept on a fiscal year basis.

Treasury Decision 2433, providing that returns may be made on a basis other than as above set forth, is not applicable to insurance companies. (Reg. 33 Rev., Art. 239.)

[Page 166.]

Gross Income. There is specifically exempted from taxation interest received on obligations of the United States or its possessions, or on the obligations of a State or any political subdivision thereof. Therefore, in ascertaining gross income for the purposes of the tax, all interest received from such sources should be eliminated. (Report to State, schedule D, parts 1 and 4.) As accrued interest on bonds purchased is not included in the interest income reported to the State insurance department, it must not be included in the amount eliminated from gross income in the return. (Report to State, schedule D, part 3.) In the case of obligations of the United States issued after September 1, 1917, income from such obligations is exempt from tax only to the extent provided in the act authorizing their issue. Income from such obligations received by insurance companies is exempt from the 2 per cent and 4 per cent income tax. (Reg. 33 Rev., Art. 239.)

[Page 174.]

Dividends Provisionally Ascertained. Dividends provisionally ascertained, apportioned, or credited on deferred dividend policies cannot be excluded or deducted from gross income for the reason that the assured has no vested or enforceable right in them and cannot, at the time of the ascertainment, apportionment, or credit, nor until the maturity of the policy, avail himself of such dividends; and in the event of the death of the assured prior to the expiration of the deferred dividend period, the amount so ascertained, apportioned, or credited lapses. (Reg. 33 Rev., Art. 241.)

[Page 175.]

Copy of Report to State. As an assistance in audit-

ing the returns, wherever possible, a copy of the report to the State insurance department should be submitted with the returns; otherwise schedule D, parts 1, 3 and 4, of the report should be attached thereto showing Federal, State, and municipal obligations from which the interest omitted from gross income was derived. (Reg. 33 Rev., Art. 239.)

[Page 175.]

Foreign Insurance Companies. Insurance companies organized, authorized, or existing under the laws of any foreign government shall report as gross income the gross amount received within the year from all sources within the United States or its possessions. Income from business transacted by a United States branch or agency of a foreign insurance company which relates to a foreign country must be returned as gross income. Otherwise articles applicable to insurance companies in general will be followed as to income and deductions.

Insurance companies organized, authorized, or existing under the laws of any foreign government, not transacting an insurance business in the United States or its possessions but receiving income from investments therein must make returns of such income, deducting therefrom the amount of such income withheld at the source. (Reg. 33 Rev., Art. 244.)

CHAPTER 14

FOREIGN CORPORATIONS

[Page 177.]

Corporations Subject to Tax. It is not necessary that the foreign corporation shall be engaged in busi-

ness in this country or that it have an office, branch, or agency in the United States. Liability to the tax attaches with respect to the income, the source of which is in the United States.

“Source” as here used means the place of the origin of the income.

Every foreign corporation having income from sources within the United States must make returns of annual net income in accordance with the rule set out in section 12 (b) of the act of September 8, 1916, as amended by the act of October 3, 1917. (Reg. 33 Rev., Art. 66.)

[Page 180.]

Foreign Governments. Section 30 of the act of September 8, 1916, as amended by the act of October 3, 1917, provides that the income of foreign Governments received from investments in the United States in stocks, bonds, or other domestic securities owned by them, or from interest on deposits in banks in the United States of money belonging to such foreign Governments, is exempt from the tax imposed by this title. This does not, however, exempt from the tax any income collected by foreign Governments from investments in the United States in stocks, bonds, or other domestic securities, which are not bona fide owned by but are loaned to such foreign Governments. The exemption here provided for is predicated upon the fact that the securities or moneys from which income is derived are actually owned by such foreign Governments. (Reg. 33 Rev., Article 87.)

[Page 181.]

Collection of the Tax at the Source. If for any reason there is included in the return which a foreign cor-

poration is required to make of all income received from sources within the United States any income upon which tax has been withheld at the source, such foreign corporation may take credit against the amount of tax due for the amount of the tax so withheld at the source; provided a statement is attached to the return setting forth the source and amount of the income upon which the tax was so withheld. (Reg. 33 Rev., Art. 201.)

CHAPTER 15

EXEMPT CORPORATIONS

[Page 194.]

Where Question as to Right of Exemption Exists. In every instance wherein exemption is conditioned upon the ground that no part of the net income received by corporations inures to the benefit of any private stockholder or individual, it will be necessary, before such organizations will be classed as exempt, for them to show to the satisfaction of the collector or the Commissioner of Internal Revenue:

- (1) The character and purpose of the organization;
- (2) The source from which all its income is derived;
- (3) What disposition is made of such incomes; and
- (4) Whether or not any of it is credited to surplus or inures or may inure to the benefit of any private stockholder or individual. (Reg. 33 Rev., Art. 78.)

[Page 197.]

Domestic Building and Loan Associations. A domestic building and loan association entitled to exemption is one organized under and pursuant to the laws of the United States or under and pursuant to the laws of

some State or Territory thereof, and which is actually carrying on for the benefit of its members a building and loan association, business in accordance with the laws under which it is organized. The fact that such an association issues fully paid or prepaid shares, calling for a specified rate of interest or dividends, will not disqualify it for exemption. The exemption is without qualification other than that the association is a domestic building and loan association. If a corporation by any other name is carrying on an exclusive building and loan business, before it is entitled to exemption it will be incumbent upon it to show to the satisfaction of the Commissioner of Internal Revenue that it is in fact a building and loan association. (Reg. 33 Rev., Art. 70.)

[Page 199.]

Cemetery Companies. A cemetery company having a capital stock represented by shares, or which is operated for profit or for the benefit of others than its members, does not come within the exempted class, and will be required to make returns of annual net income and pay any income tax thereby shown to be due.

In the case of such company a reserve set aside out of profits as a "maintenance fund" is not deductible from gross income, and any accretions to such fund will be held to be income, and as such, must be returned by the corporation. The expenses of maintenance will be deductible as they are paid. (Reg. 33 Rev., Art. 71.)

[Page 199.]

Clubs. If a club, by reason of the comprehensive powers granted in its charter, engages in traffic, in agri-

culture, or horticulture, in the sale of real estate, timber, etc., for profit, it will be held that such club is not organized and operated exclusively for pleasure, recreation, or social purposes. It thus becomes a business or commercial enterprise, and any profit realized from such activities is subject to the tax imposed by this title, and the club so operated must make returns of annual net income. (Reg. 33 Rev., Art. 72.)

[Page 201.]

Cooperative Dairies. Cooperative dairy companies or associations not having capital stock and engaged in collecting milk and disposing of the same or the products thereof, and distributing the proceeds of the business, less necessary operating expenses, among their patrons, upon the basis of the quantity of butter fat in the milk furnished by such patrons, are held to be exempt from the tax imposed by this title. (Reg. 30 Rev., Art. 76.)

[Page 202.]

Associations for Marketing Produce. Cooperative associations, in order to come within the exemption provided in paragraph "eleventh" must establish to the satisfaction of the collector or Commissioner of Internal Revenue the fact that, for their own account, they have no net income, their business being to market the products of their members, and that the entire proceeds of such marketing, less necessary selling expenses, are turned back or paid to the members on the basis of the quantity of produce furnished by them—quality and grade being considered—as the purchase price of such produce.

If in the course of their business such associations

purchase for cash at a stipulated price articles or produce with a view to selling them for gain, it will be held that such associations are organized for profit and such associations will be required to make returns of annual net income and include therein, for the purpose of the tax, all income derived from such transactions. If amounts paid to members are based solely upon the quantity of produce furnished, such amounts may be deducted from the gross proceeds of sales, and the taxable net income will be the amount of earnings passed to surplus, or distributed or distributable among members on the basis of their stock holdings. (Reg. 33 Rev., Art. 75.)

[Page 204.]

Federal Reserve Banks. Dividends paid by member banks are not exempt from tax. (Reg. 33 Rev., Art. 86.)

CHAPTER 16

INCOME—IN GENERAL

[Page 208.]

Constructive Receipt of Income. Actual receipt is a reduction to possession. Constructive receipt is where income is credited to or made available to recipients and is to be reported as income; as credit to account of recipients of savings-bank interest, etc. (Reg. 33 Rev., Art. 4.)

[Page 211.]

Inventory. Under date of December 19, 1917, the Treasury Department altered its long-established rule of permitting inventories on the basis of cost only. In T. D. 2609, issued on that date, it was held as follows:

1. For the purposes of income and excess profits tax returns, inventories of merchandise, etc., and of securities, will be subject to the following rules:

A. Inventories of supplies, raw materials, work in process of production and unsold merchandise, must be taken either (a) at cost, or (b) at cost or market price which ever is lower; provided that the method adopted must be adhered to in subsequent years unless another be authorized by the Commissioner of Internal Revenue.

B. A dealer in securities who in his books of account regularly inventories unsold securities on hand either (a) at cost, or (b) at cost or market price which ever is lower, may for the purpose of income and excess profits taxes make his return upon the basis upon which his accounts are kept provided that a description of the method employed shall be included in or attached to the return, that all the securities must be inventoried by the same method, and that such method must be adhered to in subsequent years unless another be authorized by the Commissioner of Internal Revenue.

C. Gain or loss resulting from the sale or disposition of assets inventoried as above must be computed as the difference between the inventory value and the price or value at which sold or disposed of.

2. In all other cases inventories must be taken at cost or at value as of March 1, 1913, as the case may be.

[Page 215.]

Stock Received in Exchange for Property. If a corporation sells its capital assets in whole or in part and the purchase price is paid with stock issued by the purchasing company, the purchase price will be the actual

value at the time of the stock issued in payment for such assets. (Reg. 33 Rev., Art. 101.)

[Page 216.]

Reorganization of Corporations. In a case wherein a corporation acquires from stockholders the stock of another corporation, giving in exchange therefor its own stock, it is held the transaction is one by which the corporation acquiring the stock becomes the sole stockholder of the other corporation. As a result of this transaction no income accrues to the corporation whose stock is thus acquired. Neither will any income accrue to this corporation if later the holding corporation should cause the assets of the underlying company to be transferred to it for mere nominal consideration.

If, however, one corporation buys the assets of another and issues direct to the selling company its own capital stock in payment for the assets acquired, the transaction will be treated by the selling company as a sale of its assets, and the question as to whether profit or loss results from the sale will depend upon whether or not the value of the stock taken in payment for the assets is in excess of the fair market price or value as of March 1, 1913, of the assets sold or of their cost accordingly as they were acquired by the selling company prior or subsequent to that date.

If the value of the stock is so in excess, the amount of such excess will be taxable income for the year in which the assets were sold and must be so returned.

If the excess over value as of March 1, 1913, or over cost, as the case may be, includes any surplus earned since March 1, 1913, upon which the income tax has been paid, the excess or profits resulting from the sale

may be reduced by the amount of such tax-paid surplus.

If the purchasing corporation takes over all the assets including accounts receivable, bills receivable, surplus, etc., of the selling corporation and assumes its liabilities, the amount so assumed will be considered a part of the purchase price, and to the extent that the entire purchase price exceeds the cost or value, as of March 1, 1913, as the case may be of the assets disposed, income will accrue to the selling company. (Reg. 33 Rev., Art. 124.)

[Page 221.]

Payment by Warrants. In cases wherein warrants are issued by a city, town, or other political subdivision of a State, and are accepted by the contractor in payment for public work done, the face value of such warrants must be returned as income for the year in which they are received. If, for any reason, the contractor upon conversion of the warrants into cash, does not receive and cannot recover the full face value of the warrants so returned, he may allowably deduct from gross income for the year in which the warrants are converted into cash, any loss sustained, which loss will be measured by the difference between the face value of the warrants returned as income and the amount actually received for them in cash, or its equivalent, when redeemed or disposed of. (Reg. 33 Rev., Art. 108.)

[Page 221.]

Living Quarters, Board or Lodging. Where service is rendered for stipulated price, wage, or salary and paid with something other than money, the stipulated

value of service in terms of money is the value at which the thing taken in payment is to be considered for the purpose of the income tax.

Where there is no stipulation as to the value of service and payment for service is made with something other than money, the market or reasonable value of the thing taken in payment is the amount to be included as income for the purposes of the income tax. (Reg. 33 Rev., Art. 4.)

[Page 223.]

Income Taxable in Year Received. In the case of compensation for service rendered, where no determination of compensation is had until the completion of the service, the amount received in consideration of the service is income to be accounted for as for the calendar year of its receipt.

Where the service and payment period is divided by the end of the taxable year, the compensation for the period so divided at the end of the year will be accounted for as income for the year in which payment is actually received. Where the service is compensated by fee, or is of such nature that no part of the fee or compensation becomes due until the completion of the service, the entire amount received should be income to be accounted for as for the year of receipt.

A person having a salary by the year and in addition commissions on sales, the salary to be paid at the time commissions are determined, and the determination of commissions is in the succeeding calendar year, the entire amount of salary and commission should be accounted for as income of the calendar year of receipt. (Reg. 33 Rev., Art. 4.)

[Page 226.]

Exempt Income. Where the entire income of an individual is from tax-exempt bonds and where the amount of income other than that from tax-exempt securities is less than the amount of income for which a return is required, no return of income is to be made. Interest from securities which is exempt from tax under section 4 of the Income Tax Law is not to be included in returns of income. (Reg. 33 Rev., Art. 26.)

[Page 228.]

“Paid” or “Actually Paid.” “Paid” or “actually paid,” within the meaning of this title, does not necessarily contemplate that there shall be an actual disbursement in cash or its equivalent. If the amount involved represents an actual expense or element of cost in the production of the income of the year, it will be properly deductible even though not actually disbursed in cash, provided it is so entered upon the books of the company as to constitute a liability against its assets, and provided further that the income is also returned upon an accrued basis.

If in the course of its business, a corporation credits the accounts of individuals, firms, or corporations with the amount of any expenses, interest, rentals, wages, etc., due them, thereby making them subject to the personal drawings of such creditors, or if expenses actually incurred are vouchered in definite amounts, the amounts so credited or vouchered may be treated as paid, and if the amounts so credited or vouchered are expenses incurred concurrently with and in the production of the income of the year, they may be allowably deducted therefrom.

This ruling must not be construed to allow as a
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deduction any accrued charges which if paid in cash or otherwise would not be deductible. (Reg. 33 Rev. Art. 126.)

Approved Accounting Practices. Pursuant to the foregoing provision, corporations keeping their accounts in strict accord with the methods prescribed by municipal, State, or Federal authorities, or in accord with approved standard accounting practices consistently followed from year to year, will be permitted to make their returns of annual net income on the basis of the accounts so kept, provided such systems of accounting clearly and correctly reflect the net income of each year.

Charged Against Current Earnings. All expenses, including interest, taxes, and other necessary charges, incidental and necessary to the creation or production of the gross income or properly chargeable against the same, being deductible from the gross income, whether paid in cash or entered on the books as a liability, can not, if unpaid, be carried forward to be deducted from the gross income of a subsequent year.

Each Year's Return Complete. Each year's return, both as to income and deductions therefrom, must be complete within itself. Charges, of whatever character, against income can not be cumulative. They must be deducted from the income of the year in which incurred or not at all. The expenses, liabilities, or deficit of one year can not be used to reduce the income of a subsequent year.

The deductions must in all cases be such as are authorized and within the limits fixed by law. (Reg. 33 Rev., Art. 127.)

Previous Year's Charges Not Deductible A corporation having the right under this rule to deduct all au-

thorized allowances, whether paid in cash or set up as a liability, it follows that if it does not within any year pay or accrue certain of its expenses, interest, taxes, or other charges, and makes no deduction therefor, it cannot deduct from the income of the next or subsequent year any amounts then paid in liquidation of the previous year's liabilities.

Amended Returns. If, however, a corporation discovers or detects expenses or liabilities which were due and payable during a preceding year, it will be permissible for it to make an amended return for the year to which such expense or liability applies, include such expense in the deductions of that year, and file a claim for refund for any taxes overpaid by reason of failure to deduct such expense or liability in the original return of that year.

Any system of accounting which is not consistent with the purpose and intent of the rules set out in this title, and with the general rules set out in these regulations for the ascertaining of net income, will not be accepted as a correct basis for making returns. (Reg. 33 Rev., Art. 128.)

CHAPTER 17

INCOME FROM PERSONAL SERVICES

[Page 233.]

Per Diem Allowance. The total allowance is income and there may be taken as a deduction for expense, the amount actually expended from such allowance for actual necessary traveling expenses. (Reg. 33 Rev., Art. 8.)

[Page 234.]

Compensation of Officers and Employees of a State or Political Subdivision Thereof. An individual who enters into a contract with a State, or any political subdivision thereof, for the doing of a thing or things specified by the contract, the completion of which will constitute a fulfillment of the contract on the part of such individual, is not an officer or employee of the State or political subdivision thereof within the meaning and intent of section 4 of the income tax law and the amount received by him from the State or political subdivision thereof under the terms of the contract is to be accounted for as income. (Reg. 33 Rev., Art. 4.)

CHAPTER 18**INCOME FROM BUSINESS, TRADE OR COMMERCE****[Page 237.]**

Inventory. Under date of December 19, 1917, the Treasury Department altered its long-established rule of permitting inventories on the basis of cost only. In T. D. 2609 issued on that date it was held that inventories should be taken at cost or market value which ever was the lower. The complete text of this T. D. appears on page — supra.

[Page 238.]

Income of Contracting Companies. Corporations engaged in contracting operations and which have numerous uncompleted contracts, which in some cases run for periods of several years, will be allowed to prepare their returns so that the gross income will be arrived at on the basis of completed work—that is,

on jobs which have been finally completed—any and all moneys received in payment for completed jobs will be returned as income for the year in which the work was completed. If the gross income is arrived at by this method, the deduction from gross income should be limited to the expenditures made on account of such completed contracts.

Or the percentage of profit from the contract may be estimated on the basis of percentage of completion and payments made thereon, in which case the income to be returned each year during the performance of the contract will be computed upon the basis of the expenses incurred on such contract during the year; that is to say, if one-half of the estimated expenses necessary to the full performance of the contract are incurred during one year, one-half of the gross contract price should be returned as income for that year; all under or over statements of income to be adjusted upon completion of the contract and return made accordingly.

In cases wherein contracts are fully performed in one year, although payment therefor may be deferred until the next, the income resulting from the performance of the contract shall be returned for the year in which it was actually earned and determined. (Reg. 33 Rev., Art. 121.)

[Page 239.]

Bank Discounts. In cases wherein banks or other corporations loan money by discounting bills or notes, one of two methods shall be used in determining the amount of discount that is to be reported as income, namely (1) if the bank or corporation makes a practice of crediting such discount directly to a "discount

account" or to profit and loss, and total amount thus credited during the year shall be considered income and shall be so reported, regardless of the fact that a portion of this amount may represent discount paid in advance and not then earned; (2) if the bank or corporation follows the practice of crediting such discount to an "unearned discount account," and later, as the discount becomes earned, debits the unearned account and credits an "earned discount account" with the amount so earned, the total amount credited to the "earned discount account" during the year shall be considered income and shall be so returned. The corporation having income of this character should state in a memorandum attached to its return which of the two methods was used in determining the amount of discount returned as income. (Reg. 33 Rev., Art. 114.)

CHAPTER 19

INCOME FROM FARMING

[Page 242.]

Farming Corporations. Corporations engaged in operating plantations, ranches, stock farms, poultry farms, and lands used for raising fruit, truck, etc., including orchards of all kinds, shall make their returns on the basis of the products actually marketed and sold during the year, whether such products were produced or purchased and resold.

All deductions shall be based upon the legitimate expense incident to the current year whether for the production of the present or future years, except that in a case wherein a corporation is engaged in producing crops which take more than a year from the time

of planting, to the process of gathering and disposal; the income reported and expenses deducted should be determined upon the crop basis. (Reg. 33 Rev., Art. 123.)

CHAPTER 22

INCOME FROM INTEREST

[Page 258.]

Political Subdivisions of a State. However, a district without power to exercise any governmental function, created for the purpose of making some improvement, primarily beneficial to the property located in and comprising the district, is not, within the meaning of these acts, a political subdivision of the State. Obligations issued in payment for such improvement, although guaranteed by a county, municipality, or other political subdivision of the State, are not the obligations of the State or of any political subdivision thereof; but are rather the obligations of the benefited property upon which they constitute a lien. Hence, the income derived from obligations which are a direct charge against or lien upon benefited property, is not exempt from these taxes, and must be returned as income of the recipient. (Reg. 33 Rev., Art. 84.)

CHAPTER 23

INCOME FROM DIVIDENDS

[Page 267.]

Dividends from Profits or Surplus of Prior Years. When an individual receives dividends declared from surplus of prior years, he will be required to add it to his other income for the current year as indicated

by the following illustration: Assume, for instance, that an individual is in receipt of \$20,000 of income for the year 1917 and also received in 1917 \$10,000 from dividends out of surplus and undivided profits accumulated by the paying corporation in 1916. The individual recipient will add the \$10,000 received in the form of such dividends to the \$20,000 received from other sources and will pay the supertax at the 1916 rates on the amount between \$20,000 and \$30,000. If he should also have received dividends from surplus and undivided profits accumulated in 1915, 1914 and 1913 he will add the sum of such dividends to the total of \$30,000 and pay a tax at the rates prescribed by the act of October 3, 1913, on the amount by which the total exceeds \$30,000. (See instructions on Form 1040 Revised, page 2, Schedule F.)

A corporation declaring and paying dividends out of a surplus or earnings accumulated over a period of years, should make a record in its books of the amount of dividends paid out of each year's undistributed surplus or profits, and advise the stockholders accordingly, in order that the dividends received by them may be taxed at the respective rates prevailing during the years in which the surplus or profits so distributed were earned. (Reg. 33 Rev., Art. 107.)

Dividends of foreign corporations received by citizens or residents of the United States are not to be apportioned to prior years. (Telegram from Treasury Department, dated January 30, 1918; I. T. S. 1918, Paragraph 3073.)

[Page 268.]

Dividends Deemed to Be from Most Recently Accumulated Profits or Surplus. If a corporation dis-

tributed dividends in 1917, such dividends will be deemed to have been paid from the earnings of 1917, and the recipient, if an individual, will be liable to additional tax, if any, and if a corporation, to income tax, at the rates for the year 1917, unless it is shown to the satisfaction of the Commissioner of Internal Revenue that at the time such dividends were paid, the earnings up to that time were not sufficient to cover the distribution, in which case the excess over the earnings of the taxable year will be deemed to have been paid from the most recently accumulated surplus of prior years, and will be taxed at the rate or rates for the year or years in which earned. (Reg. 33 Rev., Art. 107.)

The Treasury Department has also held that if a dividend was declared prior to August 6, 1917, out of earnings or profits accrued prior to March 1, 1913, such dividend will be deemed to be from the most recently accumulated profits or surplus unless the dividend was also paid prior to August 6, 1917. In other words, the term "distribution" as used in the law as held by the Treasury Department to mean the payment and not the declaration of dividends.

[Page 271.]

Dividends from Exempt Income. Interest on State, municipal and United States bonds received by corporations is not taxable to the corporation. Upon amalgamation with other funds of the corporation such income loses its identity. When distributed to stockholders as a dividend, the entire amount of the dividend is subject to inclusion in returns of income for the purposes of the income tax.

The foregoing holds true for scrip payment of interest. (Reg. 33 Rev., Art. 4.)

[Page 271.]

Dividends from Reserves for Depreciation or Depletion. A reserve set up out of gross receipts and maintained by a corporation for the purpose of making good any loss or wasting of capital assets on account of depreciation or depletion is not to be considered a part of the earned surplus of the company, but a reserve for the return or liquidation of capital. A dividend paid from such reserve will be considered a liquidating dividend and will not constitute taxable income to the stockholder except to the extent that the amount so received is in excess of the capital actually invested by the stockholder in the shares of stock held by him, and with respect to which the distribution was made. (Reg. 33 Rev., Art. 4.)

[Page 272.]

Dividends Paid in Equivalent of Cash. Dividends declared by a corporation and paid with securities in which the surplus of the corporation has been invested, regardless of the character of such securities, is to be accounted for as a dividend for income tax purposes by the recipients of same to the extent that it represents a distribution of surplus accrued to the corporation since March 1, 1913. (Reg. 33 Rev., Art. 4.)

[Page 274.]

Stock Dividends. The United States Supreme Court on January 7, 1918, in deciding the case of *Towne v. Eisner*, held that stock dividends were not taxable. The opinion reads in part as follows: "Notwithstanding

ing the thoughtful discussion that the case received below we can not doubt that the dividend was capital as well for the purpose of the Income Tax Law as for the distribution between tenant for life and remainderman. What was said by this Court upon the latter question is equally true for the former. 'A stock dividend really takes nothing from the property of the corporation, and adds nothing to the interest of the shareholders. Its property is not diminished and their interests are not increased. * * * The proportional interest of each shareholder remains the same. The only change is in the evidence which represents that interest, the new shares and the original shares together representing the same proportional interest that the original shares represented before the issue of the new ones.' *Gibbons v. Mahon*, 136 U. S. 549, 559, 560. In short, the corporation is no poorer and the stockholder is no richer than they were before. *Logan County v. United States*, 169 U. S. 255, 261. If the plaintiff gained any small advantage by the change it certainly was not an advantage of \$417,450, the sum upon which he was taxed. It is alleged and admitted that he received no more in the way of dividends and that his old and new certificates together are worth only what the old ones were worth before. If the sum had been carried from surplus to capital account without a corresponding issue of stock certificates, which there was nothing in the nature of things to prevent, we do not suppose that any one would contend that the plaintiff had received an accession to his income. Presumably his certificate would have the same value as before. Again if certificates for \$1,000 par were split up in ten certificates, each for \$100, we presume that no one would call the new

certificates income. What has happened is that the plaintiff's old certificates have been split up in effect and have diminished in value to the extent of the value of the new." Notwithstanding the broad language in this opinion, the Treasury Department has declared that since only the language of the 1913 Law and not the language of the 1916 Law was before the Court in this case, it does not necessarily follow that stock dividends are not taxable under the provisions of the 1916 Law and the 1917 Law. Since the 1916 Law contains an express provision taxing stock dividends, the Treasury Department will continue to be governed by this express provision and will assess the tax on such dividends unless and until the Supreme Court holds otherwise. The taxpayers against whom a tax is assessed on such dividends should exercise care in paying the tax under protest and duress in order to protect their rights to recovery. Where stock dividends are reported in the annual return of net income care should be taken that they are segregated from cash dividends and that it be clearly shown either on the return or on a rider attached to the return that the dividend was paid in stock and that the amount is reported not as an admission of liability for tax thereon, but out of courtesy for the Commissioner of Internal Revenue and in order to avoid the imposition of penalties for an alleged false or fraudulent return.

Stock Dividends Resulting from Revaluation of Assets. Stock dividends declared from a surplus created from the revaluation of capital assets or a value placed upon trademark, good will, etc., do not represent a distribution of earnings or profits subject to tax in the hands of the recipient shareholder. The entire

proceeds derived by a shareholder from the sale of such stock is income subject to both the normal and additional tax and shall be accounted for in the shareholder's return rendered for the year in which sold. (Reg. 33 Rev., Art. 4.)

CHAPTER 25

INCOME FROM MISCELLANEOUS SOURCES

[Page 281.]

Building and Loan Associations. Amount credited to shareholders of building and loan associations, when title to such credit passes to the shareholder at the time of the credit, has a taxable status for the normal and additional tax as for the year of the credit. Where the amount of such accumulations does not become available to the shareholder until the maturity of a share, the amount of a share in excess of the aggregate amount paid in by the shareholder is income to be accounted for as for the year of the maturity of the share for both the normal and additional tax. (Reg. 33 Rev., Art. 4.)

[Page 281.]

Damages. When a corporation as a result of suit or otherwise secures payment for damages which it may have sustained, and the amount of such payment is in excess of an amount necessary to make good the damage or damaged property, the amount of such excess shall be considered and returned as income for the year in which received. If the entire or an estimated amount of the damage shall have been previously charged off and deducted from gross income,

then the amount recovered shall be returned as income. (Reg. 33 Rev., Art. 94.)

[Page 285.]

Stock Received as Bonus. Where common stock is received as a bonus in consideration of the purchase of preferred stock, the common stock has no taxable status. The entire proceeds derived from the sale or transfer of such stock is income subject to the normal and additional tax. (Reg. 33 Rev., Art. 4.)

[Page 285.]

Sale of Bonds at Premium. If bonds are sold at a premium, the premium must be reported as income. (Reg. 33 Rev., Art. 150.)

CHAPTER 26

RECEIPTS WHICH ARE IN PART RETURN OF CAPITAL

[Page 292.]

Instalment Payments. Corporation selling furniture, musical instruments, clothing, furnishings, etc., on the instalment basis, title passing to the vendee at the time of sale, will treat such contracts as accounts receivable and as "sales during the year" at their face value, thus accounting for as income the difference between the cost and the sales price. If the purchaser defaults in payment and the account becomes uncollectible and the uncollected balance is charged off, the amount so charged off may be deducted as a loss. (Reg. 33 Rev., Art. 120.)

CHAPTER 27

DEDUCTIONS—IN GENERAL

[Page 299.]

Accruals. Corporations keeping books of account on an accrual basis may deduct from gross income accrued interest for the year when shown as a charge against accrued income upon the books of account. (T. D. 2625.)

[Page 302.]

Voluntary Destruction of Property. Loss due to the voluntary removal or demolition of old buildings, the scrapping of old machinery, equipment, etc., incident to renewals and replacements will be deductible from gross income, in an amount representing the difference between the cost of such property demolished or scrapped and an amount measuring a reasonable allowance for the depreciation which the property had undergone prior to its demolition or scrapping; that is to say, the deductible loss is only so much of the original cost, less salvage, as would have remained unextinguished had a reasonable allowance been charged off for depreciation during each year prior to its destruction.

When a corporation buys real estate, upon which is located a building or buildings, which it proceeds to raze, with a view to erecting thereon another building or buildings, it will be held that the corporation has sustained no deductible loss by reason of the demolition of the old building or buildings. In such case it will be considered that the value of the real estate, exclusive of old improvements, is equal to the pur-

chase price of the land and buildings. (Reg. 33 Rev., Arts. 155 and 156.)

[Page 303.]

Investment of Capital. Investments of capital are not deductible. The following have been held to be investments of capital and not expenses: (a) Amounts expended for securing copyright and plates which remain in possession of and as property of the person making the payments, are investments of capital and can not be allowed as deductions in returns of income. (b) Cost of defending title or perfecting title to property, constitutes a part of the cost of the property and is not a business expense. (c) The amount expended for architect's services is part of the cost of the building and not a deductible business expense. (d) Commissions paid in purchasing and selling securities are a part of the cost or selling price of the securities and not otherwise deductible. They do not constitute expense deductions in a return of income. (Reg. 33 Rev., Art. 8.)

CHAPTER 28

DEDUCTION OF BUSINESS EXPENSES

[Page 306.]

Sums Expended for Materials Used and on Hand. If a corporation carries materials or supplies on hand for which no record of consumption is kept or of which physical inventories at the beginning and end of the year are not taken, it will be permissible for the corporation to include in its expenses and deduct from gross income the total cost of such supplies and ma-

terials as were purchased during the year for which the return is made. (Reg. 33 Rev., Art. 130.)

[Page 306.]

Commissions. Commissions paid in purchasing and selling securities are a part of the cost or selling price of the securities and not otherwise deductible. They do not constitute expense deductions in a return of income. (Reg. 33 Rev., Art. 8.)

[Page 307.]

Redemption of Trading Stamps. Corporations, mercantile or otherwise, which issue trading stamps, coupons, etc, for the purpose of increasing their business, which stamps or coupons are redeemable in merchandise, may allowably deduct from gross income as a business expense the amount which such corporations actually expend for such stamps or coupons, and also the actual cost to the corporations of the merchandise given in redeeming the same. This rule contemplates that a reserve set up as a liability equal to the redemption value of the stamps or coupons issued is not, as such, an allowable deduction, the deduction being limited to the cost of the stamps or coupons and the merchandise with which they are redeemed. (Reg. 33 Rev., Art. 141.)

[Page 311.]

Rent for Residential Property. In the case of a professional man who rents a property for residential purposes but receives there clients, patients, or callers in connection with his professional work (the place of business being elsewhere) no part of the rent is deductible as business expense. (Reg. 33 Rev., Art. 8.)

[Page 312.]

Life Insurance Premiums. The provision of Section 32 of the Act of September 8, 1916, that premiums paid on life insurance policies covering the lives of officers, employees, or those financially interested in any trade or business conducted by an individual, partnership, or corporation, may not be deducted as a part of the annual expense, applies to all forms of life insurance, the premiums upon which the individual, partnership or corporation may pay who ever may be the beneficiaries. (Reg. 33 Rev., Art. 236.)

[Page 315.]

Allowances to Minor Children. The father is legally entitled to the service of his minor children. As a rule, allowances which he gives them, whether said to be in consideration of service or otherwise, are not allowable deductions, in his return of income nor are they income to the children. (Reg. 33 Rev., Art. 8.)

[Page 315.]

Bonus and Profit Sharing Payments. The earlier rulings on this subject have been modified by a recent decision which holds that special payments, sometimes denominated *gifts* or *bonuses*, made by corporations, partnerships, or individuals to officers or employees, will constitute allowable deduction from gross income in ascertaining net income for the purpose of the income tax, when such payments are made in good faith and as additional compensation for the services actually rendered by the officers or employees. If such payments, when added to the stipulated salaries do not exceed a reasonable compensation for the services rendered, they will be regarded as a part of the wage or hire of the officer or employee, and therefore an ordi-

nary and necessary expense of operation and maintenance, and as such will be deductible from gross income.

Special payments made to officers or employees, although in the form of additional salaries or compensation, will be regarded as a special distribution of profits or compensation for the capital invested, and not as payment for services rendered, if the amount of such payments is based upon or bears a close relationship to the stock holdings of such officers or employees, or to the capital invested by them in the business. Payment under such latter conditions being in the nature of dividends or distribution of profits will not be deductible from gross income.

Salaries of officers or employees, who are stockholders or have an interest in the business, will be subject to careful analysis, and if they are found to be rather in proportion to the stock holdings or interest of such officers and employees than to the real value of the services rendered and to be in excess of the salaries paid to officers or employees in similar positions in other concerns doing business of a like nature and of approximately equal volume and earnings, the amount paid in excess of reasonable compensation for the services will not be deductible from gross income, but will be treated as a distribution of profits. (T. D. 2616; Reg. 33 Rev., Art. 8.)

In one case it was held that a distribution by a corporation of 10% of its net earnings to employees in addition to their regular salaries or wages was a proper deduction from gross income if the distribution was made for services actually rendered and was not such a distribution of profits as would be covered by the terms "gratuity" or "free bonus" (Letter from Treasury Department dated November 12, 1917; I. T.

S. 1917, Paragraph 2481.) A profit sharing or bonus payment, however, is not in any event allowed as a deduction if the amount is left on deposit with the company to secure the company against such losses as may be charged to the employees. (Letter from Treasury Department dated November 30, 1917.)

[Page 317.]

Pensions. No deduction shall be made for contributions to a pension fund the resources of which are held by the corporation, the amount deductible in such case being the amount actually paid to the employee. (Reg. 33 Rev., Art. 136.)

[Page 318.]

Farmers. Amounts expended in the development of orchards and ranches prior to the time when the productive stage is reached are considered as investments of capital and are not deductible as expense. (Reg. 33 Rev., Art. 4.)

CHAPTER 29

DEDUCTION OF INTEREST

[Page 323.]

Accrued Interest. Corporations keeping books of account on an accrual basis may deduct accrued interest for the year whether paid or not when shown as a charge against accrued income upon the books of account. (T. D. 2625.)

CHAPTER 31

DEDUCTION OF LOSSES

[Page 337.]

Issue of Bonds Below Par. Where a railroad company sold bonds and equipment notes at a discount in

1906 and the books show that the loss was entirely charged off under the profit and loss account for 1906, and the company in making returns of excise tax for the years 1911 and 1912 failed to deduct the proportionate amount of discount sustained, it has no right to claim refund of such amount. (Chicago and Alton Railroad Company v. U. S. Court of Claims, decided December 3, 1917; D. T. 2631.) If the bonds were sold subsequent to January 1, 1909, at a discount, and the amount of the discount was then charged off on the books, either against earnings or surplus, but not deducted in the corporation's return of net income, such discount as was not then deducted in its entirety, may be spread over the life of the bond, and an aliquot part of the discount may be deducted from the gross income of each year until the bonds mature or are redeemed.

In cases wherein a corporation sells its bonds at a discount plus a commission for selling the amount of such discount and commission, together with other expenses incidental to issuing the bonds, constitutes a loss, the aggregate amount of which loss will, for the purpose of an income tax return, be prorated over the life of the bonds sold, and the amount thus apportioned to each year will be deductible from the gross income of each such year until the bonds shall have been redeemed.

If a corporation having sold its bonds at a discount, the discount having been deducted from gross income later repurchases or redeems the bonds at a price less than par, the difference between the price at which they are redeemed and their par value will be returned as income. (Reg. 33 Rev., Art. 150.)

[Page 339.]**Loss by Destruction or Disappearance of Property.**

When the loss is claimed through the destruction of property by fire, flood, or other casualty the amount deductible will be the difference between the value as of March 1, 1913, or the cost of the property and the salvage value thereof, including in the latter value the amount, if any, that has been or should have been set aside and deducted in the current or previous years from gross income on account of depreciation and which has not been paid out in making good the depreciation sustained. (Reg. 33 Rev., Art. 147.)

[Page 343.]

When Debts May be Considered Worthless. Where an indebtedness is claimed and contested and a settlement is had by way of compromise whereby an amount, less than the debt claimed, is accepted in full payment and satisfaction of the debt, the difference between the amount paid and that claimed is not allowable as a deduction for bad debts. Where the settlement in compromise consists of a promise to pay an amount less than the debt claimed, the amount promised to be paid forms the basis of a new transaction, and upon failure to make good this promise the question will arise as to the deductibility of the new amount only.

Where all of the surrounding and attendant circumstances indicate that a debt is worthless and uncollectible and that legal action to enforce payment would in all probability not result in the satisfaction of execution on a judgment, a showing of these facts will be sufficient showing of the worthlessness of the debt for purposes of deduction.

Where, under foreclosure, a mortgagee buys in the mortgaged property and credits the indebtedness with the purchase price the difference between purchase price and the indebtedness will not be allowable as a deduction for bad debt—the property which was security for the debt being in possession and ownership of the mortgagee is, for the purposes of income tax, held to be sufficient to justify a disallowance of a claim for bad debt. Only where purchaser for less than debt is another than mortgagee may the difference between debt and net from sale credited be deducted as bad debt. (Reg. 33 Rev., Art. 8.)

It is not essential that the bad debt or account shall be proved worthless by legal proceedings before the deduction may be allowed but the corporation must not only be satisfied that the debt or account is worthless, but must be able to satisfy the Commissioner or Collector of Internal Revenue that the accounts charged off were definitely determined at the time to be worthless and that they had not been recognized as worthless or without value prior to the beginning of the year for which the return is made. (Reg. 33 Rev., Art. 151.)

[Page 344.]

Loss Due to Adverse Judgment. Amounts paid pursuant to judgment or otherwise on account of damages are deductible from gross income in the year and to the extent such amounts are actually paid, less any amount of such damages as may have been compensated for by insurance. (Reg. 33 Rev., Art. 158.) If on suit for damages the amount recovered is less than the damage sustained or less than an amount necessary to make good the damage the difference between the actual amount of damage sustained and the amount

recovered will be deductible as a loss. (Reg. 33 Rev., Art. 94.)

[Page 345.]

Cost of Drawings, Models and Patterns. Expenditures made for designs, drawings, patterns or models representing work of an experimental nature should be treated as a capital disbursement and not as an expenditure if the designs, drawings, patterns or models prove to be satisfactory and result in the production of salable goods. If, however, they prove to be unsatisfactory and have no asset value, the expenditure may be charged off as a loss incident to running the business and as such deducted from gross income, provided that the taxpayer is taking credit for such expenditures in the income tax return makes a full and complete explanation with respect to the same and to the satisfaction of the Commissioner of Internal Revenue. (Reg. 33 Rev., Arts. 175 and 176.)

If designs, drawings, patterns, or models result in the production of goods which prove to be salable for a certain length of time and then become obsolete and can not be sold, the amount expended for such designs, drawings, patterns, or models, less any amounts previously claimed as depreciation with respect to the same or as a return of capital, may when charged off, be included in, and deducted as a loss incident to running the business, provided full and complete information is reported in a manner satisfactory to the Commissioner of Internal Revenue. (Reg. 33 Rev., Art. 177.)

Obsolescence Deductible, Cost Less Depreciation and Salvage. Amounts representing losses on account of obsolescence of physical property may be included

as a deduction from gross income as a loss, provided such amounts have been recorded in the books following the condemnation and withdrawal from use of the obsolete property. The amount of obsolescence that may be claimed as a deduction shall be ascertained by deducting from the cost of the property the total amount that has been previously claimed and deducted on account of the depreciation of the property, plus residual value at time of obsolescence, or plus the amount received from the sale of the property. The obsolescence deduction must not include the accumulated depreciation applicable to prior years. (Reg. 33 Rev., Art. 178.)

Obsolescence When no Depreciation is Deducted. If no depreciation has been charged off against such property and deducted from gross income of prior years, the amount allowable as a deduction for the year in which the property becomes obsolete shall be ascertained by deducting from the cost of the property its residual value plus an amount equal to the depreciation actually sustained during the prior period and which might have been deducted when computed at the rate applicable to the same or similar property. The amount of depreciation thus arrived at as applicable to former years may be made the basis of amended returns and a claim for the refund of taxes overpaid by reason of the fact that no depreciation deduction was claimed in those years. (Reg. 33 Rev., Art. 179.)

Loss on Inventory by Obsolescence or Damage. No deductions from the inventory value of merchandise or material will be allowed except in cases in which the inventory includes goods or materials which by reason of obsolescence or damage are unsalable. When such deduction is claimed the facts connected there-

with, including a statement of the cost of the goods, the value at which they were inventoried, and their present condition, must be filed with the return. (Reg. 33 Rev., Art. 160.)

CHAPTER 32

DEDUCTION FOR ALLOWANCE FOR DEPRECIATION

[Page 348.]

Merchandise. Depreciation computed on total invoice cost of merchandise in stock is not an allowable deduction, except that if any portion of the merchandise in stock is unsalable by reason of obsolescence or damage, a depreciation deduction not in excess of the decline in value during the taxable year will be allowed. (Reg. 33 Rev., Art. 169.)

[Page 355.]

Rate of Depreciation. If it develops that by reason of underestimating the life of the property or by overestimating the rate of deterioration an amount in excess of the yearly depreciation has been taken, the rate applicable to future years should at once be reduced and the balance of the cost of the property not provided for through a depreciation reserve should be spread over the estimated remaining life of the property. (Reg. 33 Rev., Art. 165.)

[Page 355.]

Annual Allowance Must be Entered on Books. Within the purview of this item depreciation, to an amount measuring the decline in value due to exhaustion, wear and tear of property arising out of its use, is a loss.

This loss, in order to constitute an allowable deduction from gross income, must be charged off. The particular manner in which the amount shall be charged off is not material, except that the amount measuring a reasonable allowance for depreciation must be either deducted directly from the book value of the assets or credited to a depreciation reserve account, and as such shall be reflected in the annual balance sheet. (Reg. 33 Rev., Art. 159.)

[Page 358.]

Diversion of Fund. If a corporation at the end of the year finds it has a certain net income, and, without making any provision for depreciation, distributes such net income among its stockholders as dividends, it will be estopped from claiming in its returns of annual net income for such year any deduction on account of depreciation unless it is shown conclusively that the property account has been reduced by the amount of depreciation claimed, or unless such amount has been credited to a depreciation reserve account, and such amount was in fact a reasonable allowance.

The depreciation allowance authorized by section 12 is intended to provide a fund out of which the loss due to use, wear, and tear may be made good, and the fund thus created can not be diverted to the payment of dividends; that is to say, a deduction made under the guise of depreciation can not measure a loss and at the same time be used in the payment of dividends.

The fact that no reserve was made for depreciation indicates that there is no loss on this account to be provided for. (Reg. 33 Rev., Art. 161.)

CHAPTER 33

DEDUCTION OF ALLOWANCE FOR DEPLETION OF OIL
AND GAS DEPOSITS

The rulings relating to depletion of oil and gas deposits have been very materially changed. Under the new rulings depletion is allowed to lessees as well as owners in fee and the amount of the annual allowance may be measured by the number of units removed from the deposit instead of by the reduction in flow and production. Regulations 33 Revised, Articles 170 to 172 inclusive, are in full as follows:

Art. 170. Oil and Gas Properties.—Sections 5 and 12 of the act of September 8, 1916, as amended by the act of October 3, 1917, authorize individuals and corporations owning and operating gas or oil properties, to deduct from gross income—

“A reasonable allowance * * * for actual reduction in flow and production, * * * provided that when the allowance authorized * * * shall equal the capital originally invested, or in case of purchase made prior to March 1, 1913, the fair market value as of that date, no further allowance shall be made.”

The essence of this provision of law is that the owner or operator of this character of properties shall secure through an aggregate of annual depletion deductions, the return of the amount of capital actually invested, or an amount not in excess of the fair market value as of March 1, 1913, of the properties owned prior to that date.

For the purpose of determining the amount of capital to be returned through annual deductions, operators may be divided into two classes, (a) operators who own the fee, and (b) operators who own a lease or leases.

In the case of the operating fee owner, the amount

returnable through depletion deductions is the fair market value of the property (exclusive of the cost of physical property) as of March 1, 1913, if acquired prior to that date, or the actual cost of the property if acquired subsequent to that date, plus, in either case, the cost of velopment (other than the cost of physical property incident to such development) up to the point at which the income from the developed territory equals or exceeds the deductible expenses.

In the case of a lessee, the capital thus to be returned is the amount paid in cash or its equivalent as a bonus or otherwise by the lessee for the lease, plus also all expenses incurred in developing the property (exclusive of physical property (prior to the receipt of income therefrom sufficient to meet all deductible expenses, after which time as to both owner and lessee, such incidental expenses as are paid for wages, fuel, repairs, hauling, etc., in connection with the drilling of wells and further development of the property, may, at the option of the operator, be deducted as an operating expense or charged to capital account.

If, in exercising this option, the individual or corporation charges the expense of drilling wells or further development to capital account, the same, in so far as such expense is represented by physical property, may be taken into account in determining a reasonable allowance for depreciation during each year until the property account thus augmented has been extinguished through annual depreciation deductions, after which no further deduction on this account will be allowed. In the case of a going or producing business, the cost of drilling non-productive wells may be deducted from gross income as an operating expense.

Estimate of Probable Resources. In the case of either an owner or lessee it will be required that an estimate, subject to the approval of the Commissioner of Internal Revenue, shall be made of the probable quantity of oil or gas contained in or to be recovered from the territory with respect to which the investment is made. The invested capital (value as of Mar. 1, 1913, or cost, if acquired subsequent to that date, plus the cost of development, other than cost of physical property, up to the point of expense-paying production, in the case of an owner, and the amount actually paid for the lease plus cost of development, other than cost of physical property, up to the same point, in the case of a lessee) will be divided by the number of units of oil or gas so estimated to be contained in or to be recovered from the territory, and the quotient will be the per unit cost or amount of capital invested in each unit recoverable. This quotient, or per unit cost, when multiplied by the number of units removed from the territory during any one year, will determine the amount which may be allowably deducted from the gross income of that year on account of depletion of assets or as a return of invested capital until the total of such deductions shall equal the capital invested.

Every individual or corporation entitled to a deduction on account of the depletion of the property under operation or for a return of the capital invested with respect to the same shall keep an accurate ledger account, in which, in the case of fee owner, shall be charged the fair market value as of March 1, 1913, or the cost, if acquired subsequent to that date, of the oil or gas property, plus cost of development as hereinbefore defined, or, in the case of a lessee, the amount actually originally invested in the lease and its development. This account shall be credited with the amount claimed and allowed

each year as a deduction on account of depletion or as a return of capital, to the end that when the credits to the account equal the debits no further deduction on either account, with respect to this property and the capital invested therein, will be allowed. Or, in lieu of a direct credit to property account, the amount so claimed and allowed as a deduction may be credited to a depletion reserve account.

Where Resources Are Uncertain. If for any reason the quantity of oil or gas in the property can not be determined with any degree of certainty, the depletion deduction will be computed in accordance with the rule set out in Treasury Decision 2447, except that lessees may compute their deduction for return of capital (cost of lease and development) in the same manner as owners in fee; that is, they may extinguish such capital on the basis of the reduction in flow and production as compared with the preceding year, or, in the case of leasehold properties brought in or developed during the year, the depletion deduction may be computed on the basis of the decline in settled flow and production, as evidenced by tests and gauges made at the end of the year as compared with similar tests and gauges made at the time the settled flow was determined.

For the purpose of computing the depletion the territory comprehended in a given lease will be considered the unit with respect to which the depletion deduction may be claimed and allowed.

If the operator is the owner of the fee the value determined and set up as of March 1, 1913, or the cost of the property if acquired subsequent to that date, or, if the operator is a lessee, the amount actually paid for the lease, plus, in the case of both owner and lessee, the cost of subsequent development, exclusive of physical prop-

erty, if such cost is capitalized, will be the basis for determining the depletion deduction or the deduction for return of capital for all subsequent years during the continuance of the ownership under which the value was fixed or by which the investment was made, and during such ownership there can be no revaluation for the purpose of this deduction if it should be found that the quantity of oil or gas in the property was underestimated at the time the value was fixed or the property was acquired, or at the time the lease contract was entered into or purchased.

This rule will not, however, be so construed as to forbid an operator from redistributing, the invested capital over the estimated number of units remaining in the territory under operation if a subsequent increase of invested capital should render this necessary in order to determine the amount of such capital applicable to each unit, provided that when such redistribution is made the total capital invested will be reduced by the amount previously charged off and deducted on account of depletion or as a return of capital.

Additional Depreciation for Machinery, Etc. Both owners and lessees operating oil or gas properties will, in addition to and separate from the deduction allowable for the depletion or return of capital as hereinbefore provided for, be permitted to deduct a reasonable allowance for depreciation of physical property, such as machinery, tools, equipment, pipes, etc. the amount deductible upon this account to be such an amount, based upon its capitalized value (cost) equitably distributed over its useful life, as will bring it to its true salvage value when no longer useful for the purpose for which such property was acquired.

As to both fee owner and lessee, the capital invested

in physical property, upon which the depreciation deduction is computed, should be segregated in the books of account from that invested in the oil or gas territory or in the lease or leases, with respect to which the deduction for depletion or return of capital is claimed, and credits for depreciation may be made in the same manner as hereinbefore provided for depletion.

Statement Required. To each return made by an individual or corporation owning and operating oil or gas properties there should be attached a statement showing—

(1) (a) The fair market value of the property (exclusive of machinery, equipment, etc.) as of March 1, 1913, if acquired prior to that date, or (b) the actual cost of the property if acquired subsequent to that date;

(2) How the fair market value as of March 1, 1913, was ascertained;

(3) The estimated quantity of oil or gas in the sand at the time the value or cost was determined;

(4) Amount of capital applicable to each unit;

(5) The quantity of oil or gas produced during the year for which the return is made;

(6) Any other data which would be helpful in determining the reasonableness of the depletion deduction.

If the operator is a lessee that fact should be stated, and to the return made by such lessee there should be attached a statement showing—

(1) The amount of cash or its equivalent actually paid for the lease;

(2) The amount expended for development prior to the receipt of income from the output, sufficient to pay operating expenses;

(3) The total capital thus invested;

(4) The estimated quantity of oil or gas in the territory comprised in the lease;

(5) The amount of capital applicable to each unit;

(6) The number of units removed during the year for which the return is made and other data that would be helpful in determining whether or not the deduction made for the return of capital is a reasonable allowance.

Art. 171. Mining Corporations. — Paragraphs "seventh" and "eighth" of section 5 (a) and paragraph "second" of section 12 (a) of Title I of the act of September 8, 1916, authorize individuals and corporations to deduct from gross income "a reasonable allowance for exhaustion, wear and tear of property, and * * * (b) in the case of mines, a reasonable allowance for depletion thereof not to exceed the market value in the mine of the product thereof which has been mined and sold during the year for which the return and computation are made;" provided, that when the sum of the annual allowances for depletion equals the capital originally invested, or in case of purchase prior to March 1, 1913, the fair market value as of that date of the mineral "in place," no further allowance on this account shall be made.

Ownership of the mine content at the time for which computation is made is an essential prerequisite to an allowable deduction for depletion.

The deduction in the case of a lessee will be limited to an amount equal to the capital actually invested in the lease, without regard to value as of March 1, 1913, or any other date.

The paragraphs of the title above referred to authorizes in the case of mine owners two classes of deductions to take care of the wasting of assets, namely, (a) depreciation, (b) depletion.

Art. 172. Deductions and Valuation.—If the property was acquired by purchase or otherwise (other than by lease) prior to March 1, 1913, the amount of invested capital which may be extinguished through annual depletion deductions from gross income will be the fair market value of the mine property so acquired, as of March 1, 1913. The value contemplated herein as the basis for depletion deductions authorized by this title must not be based upon the assumed salable value of the output under current operative conditions, less cost of production, for the reason that the value so determined would comprehend the profits to be realized from operation of the property.

Neither must the value determined as of March 1, 1913, be speculative, but must be determined upon the basis of the salable value *en bloc* as of that date of the entire deposit of minerals contained in the property owned, exclusive of the improvements and development work; that is, the price at which the natural deposits or mineral property as an entirety in its then condition could have been disposed of for cash or its equivalent.

The *en bloc* value having been thus ascertained, an estimate of the number of units (tons, pounds, etc.) should be made. The *en bloc* value divided by the estimated number of units in the property will determine the per unit value, or amount of capital applicable to each unit, which, multiplied by the number of units mined and sold during any one year, will determine the sum which will constitute an allowable deduction from the gross income of that year on account of depletion.

Deduction computed on a like basis may be made from year to year during the ownership under which the value was determined, until the aggregate *en bloc* value as of March 1, 1913, of the mine or mineral deposits shall

have been extinguished, after which no further deduction on account of depletion with respect to this property will be allowed to the individual or corporation under whose ownership the *en bloc* value was determined.

Fair Market Value, March 1, 1913. The precise detailed manner in which the estimated fair market value of mineral deposits as of March 1, 1913, shall be made must naturally be determined by each individual or corporation interested, and who is the owner thereof, upon such basis as must not comprehend any operating profits, the estimate in all cases to be subject to the approval of the Commissioner of Internal Revenue.

In any case in which a corporation uses for purposes of its income return an estimate of the value of mines or of mineral lands or properties as of March 1, 1913, as the basis of computing amounts to be deducted for depletion or return of capital, this department in passing upon the accuracy and fairness of such estimate will attach due weight to the market value of the stock of the corporation on March 1, 1913, and also to sworn statements as to the value of capital stock of the corporation filed at any time thereafter for purposes of the special excise tax on corporations based on value of their capital stocks imposed by Title IV of the Act of September 8, 1916.

In any case in which any depletion deduction is computed on the basis of the cost or price at which any mine, mineral lands or properties were acquired; the corporation will be required upon request of the Commissioner of Internal Revenue to show that the cost or price at which the property was bought was fixed for purposes of a bona fide purchase or sale by which the property passed to an owner in fact as well as in form, different from the vendor. No fictitious or inflated cost or price will be per-

mitted to form the basis of any calculation of a depletion deduction, and in determining whether or not the price or cost at which any purchase or sale was made represented the actual market value of the property sold due weight will be given to the relationship or connection existing between the party or parties selling the property and the buyer thereof.

Records to be Kept. Every individual or corporation claiming and making a deduction for depletion of natural deposits shall keep an accurate ledger account, in which shall be charged the fair market value as of March 1, 1913, or the cost, if the property was acquired subsequent to that date, of the mineral deposits involved. This account shall be credited with the amount of the depletion deduction claimed and allowed each year, or the amount of the depletion shall be credited to a depletion reserve account, to the end that when the sum of the credits for depletion equals the value or cost of the property no further deduction for depletion with respect to this property will be allowed. The value determined and set up as of March 1, 1913, or the cost of the property if acquired subsequent to that date will be the basis for determining the depletion deduction for all subsequent years during the ownership under which the value was fixed, and during such ownership there can be no revaluation for the purpose of this deduction if it should be found that the estimated quantity of the mineral deposit was understated at the time the value was fixed or at the time the property was acquired.

In cases wherein the quantity of the mineral deposit in the mine prior to March 1, 1913, can not be estimated with any degree of accuracy, it will be necessary, if depletion deductions are to be taken, for the individual or corporation owning the deposits, with the best infor-

mation available, to arrive at the fair market value of the property as of March 1, 1913; that is, its fair cash value *en bloc*, if such value is believed to be other than its original cost, which value, during the period of the ownership under which it was determined, shall be final and shall be charged to the property account as hereinbefore indicated, and then, on the basis of the most probable number of units in the property, the per unit value shall be determined as the basis for computing annual depletion allowances, this method and allowances to be continued until, but not beyond, the time when the value as of March 1, 1913, shall have been extinguished.

When to Use Original Cost Basis. The original cost of the mineral deposit may be taken as the basis for computing annual depletion deductions if the fair market value as of March 1, 1913, as hereinbefore required, can not be ascertained otherwise, allowance being made for minerals which may have been removed prior to that date.

In cases wherein a mineral property was acquired subsequent to March 1, 1913, the same rule for computing the annual depletion deduction will apply, except that in such case the basis of the computation will be the actual cost rather than the value as of March 1, 1913.

A lessee corporation is not entitled to any depletion deduction as such, but if such lessee, in addition to royalties, pays a stipulated sum for the right to explore, develop, and operate a mine, such sum may be spread ratably over the estimated number of units in the mine, to thus ascertain the amount of invested capital or bonus payment applicable to each unit. The per unit cost thus ascertained will be multiplied by the number of units removed from the mine during any one year and the result will be the amount that may be deducted from the gross income of that year as a return of the capital in-

vested. In the case of both mine owner and lessee no deduction for depletion or return of capital will be allowed when the invested capital has through the aggregate of all such deductions been extinguished.

Lessee's Computation of Invested Capital. For the purpose of computing this deduction in the case of a lessee company, the actual amount of the bonus payment and not a value as of March 1, 1913, will be considered the invested capital to be returned through the aggregate of the annual deductions.

To the return made pursuant to the above rule there should be attached a statement setting out (1) whether the operator is a fee owner or lessee; (2) in the case of a fee owner (a) the fair market value of the mineral deposits as of March 1, 1913, if the property was acquired prior to that date, (b) the cost of the mineral property if acquired subsequent to that date; (3) the method by which the value as of March 1, 1913, was determined, in case the property was acquired prior to that date; (4) the estimated quantity in units in the mine as of March 1, 1913, or at the date of purchase if acquired subsequent to that date; (5) amount of capital applicable to each unit; (6) the number of units removed and sold during the year for which the return was made; and (7) any other data which would be helpful in determining the reasonableness of the depletion deduction claimed in the return.

In the case of a lessee, the statement should show (a) the amount of the bonus or other payment made for the right to operate the mine; (b) the period covered by the lease, and the estimated quantity of units in the mine when the lease contract was entered into.

In addition to the deduction hereinbefore provided for, the operator will be permitted to deduct from the

gross income of each year a reasonable allowance for depreciation of all physical property used in connection with the operation of the mine, and owned by the operator. For this purpose the actual cost (not value) will be equitably distributed over the useful life of such property until the true salvage value has been reached.

Both owner and lessee will keep accurate ledger accounts to which will be charged the capital invested in the mine or lease and in machinery, equipment, etc., crediting such accounts or a depletion and depreciation reserve account, with the amount claimed and allowed as a deduction each year until as a result of such credits the capital charge shall be extinguished, after which no further deduction on these accounts will be allowed.

CHAPTER 34

DEDUCTION OF ALLOWANCE FOR DEPLETION OF MINES

In the new regulations the subject of depletion of mines is treated together with the subject of depletion of oil and gas wells. The regulations are printed in full on pages 724 to 729 in this supplement.

CHAPTER 35

RETURN OF ANNUAL NET INCOME

[Page 382.]

By Whom Filed. Returns are required of all unmarried persons of lawful age having a net income of \$1,000 or over. And of all married persons having a net income of \$2,000 or over. Heads of families who are married will be required to make returns of income when having

a net income of \$2,000 or over. Heads of families who are unmarried will be required to make returns of income when having a net income of \$1,000 or over, though the basic exemption which may be claimed in a return of income will be \$2,000. Under the Act of September 8, 1916, as amended, the Act of October 3, 1917, returns will be required in the case of net incomes equal to or in excess of \$1,000 or \$2,000, according to the marital status of the person making the return. (Reg. 33 Rev., Art. 26.)

[Page 383.]

Husband and Wife. Where husband and wife file separate returns of income, one of them being filed in time and the other delinquent, such returns are not supplemental of each other and delinquency must be answered for by the one in connection with whose return it occurred. (Reg. 33 Rev., Art. 26.)

[Page 385.]

When Filed. The time for filing all returns due after October 16, 1917, and on or before March 1, 1918, under the Act of September 8, 1916, and the Act of October 3, 1917, for income and excess profits taxes, whether made on the basis of the calendar year or of a fiscal year ended during the year 1917, is extended to April 1, 1918. (T. D. 2650.) This includes returns of information at the source and withholding at the source and returns by individuals and corporations.

[Page 389.]

Verification Abroad. Income tax returns executed abroad may be attested free of charge before United States consular officers. Where a foreign notary or

other official having no seal shall act as attesting officer, the authority of such attesting officer should be certified to by some judicial official or other proper officer having knowledge of the appointment and official character of the attesting officer. (Reg. 33 Rev., Art. 26.)

[Page 394.]

Returns of Fiduciaries. An executor acts for his principal and not for the beneficiaries of the estate of his principal. Beneficiaries are not entitled, as such, to an inspection of returns of income filed by such executor. (Reg. 33 Rev., Art. 26.)

CHAPTER 36

ASSESSMENT AND PAYMENT OF THE TAX

[Page 404.]

Advance Payment of Tax. As to the method of computing the tax to be paid in the case of advance payments, the Treasury Department has issued the following instructions:

If taxpayers elect to make advance partial payments on their income or excess profits taxes, or both, as provided by Section 1009 of the Act of October 3, 1917, at least one-fourth of the estimated tax due must be paid within thirty days after the close of the taxable year, at least an additional fourth within two months after the close of the taxable year, at least an additional fourth within four months after the close of the taxable year, and the remainder of the tax due on or before the time now fixed by law for such payment. For the first taxable year, this means in the case of partnerships and corporations who do not fix their own fiscal years and in

the case of individuals that at least one-fourth of the estimated tax due must be paid on or before January 30, 1918, at least an additional fourth on or before February 28, 1918, at least an additional fourth on or before April 30, 1918, and the remainder of the tax due on or before June 15, 1918. In the case of a partnership or corporation whose fiscal year ends July 31, for example, at least one-fourth of the estimated tax due must be paid on or before August 30, at least an additional fourth on or before September 29, at least an additional fourth on or before November 28, and the remainder of the tax due on or before January 12, 165 days after the close of its fiscal year. Taxpayers are not allowed under these regulations to make advance payments in installments or in whole before the close of their taxable year. Upon the first three installments, interest at the rate of 3% per annum (365 days) will be allowed from the date each payment is made to the date now fixed by law for such payment. If the final payment is made within $4\frac{1}{2}$ months after the close of the taxable year, interest at the rate of 3% per annum (365 days) will be allowed from the date of payment to the date now fixed by law for such payment.

In arriving at the amount of the fourth installment required to satisfy the assessed tax, it will be necessary to find the difference between the assessed tax and the sum of the first three installments and the interest at 3% per annum (365 days) on same from the dates of payment to the date now fixed by law for such payment. This difference will be the amount of the fourth installment, if said installment is paid after the expiration of $4\frac{1}{2}$ months after the close of the taxable year, since Sec. 1009 provides that no credit for interest shall be allowed on payments in excess of taxes determined to

be due, nor on payments made after the expiration of $4\frac{1}{2}$ months after the close of the taxable year.

If the fourth installment is paid before the expiration of $4\frac{1}{2}$ months after the close of the taxable year, the amount of such installment will be found by dividing the difference mentioned in the preceding paragraph by 1.00 plus the interest at 3% per annum (365 days) on \$1 for the number of days from the date on which said fourth installment is paid to date now fixed by law for such payment.

For example, a taxpayer on January 15, 1918, files an income or excess profits tax return showing a tax liability of \$4,000 and with the return makes partial payment of \$1,000; February 25, 1918, makes a second payment of \$1,000; March 25, 1918, a third payment of \$1,000; and the balance May 1, 1918.

The first payment draws interest at the rate of 3% per annum from January 15 to June 15, 151 days (in January, 16; February, 28; March, 31; April, 30; May, 31; and June, 15), or \$12.41, amount \$1,012.41; the second payment, 110 days (February, 3; March, 31; April, 30; May, 31; and June, 15), or \$9.04, amount \$1,009.04; and the third payment, 82 days (March, 6; April, 30; May, 31; and June, 15), or \$6.74 (\$6.739), amount \$1,006.74. The sum of the three payments and interest thereon is \$3,028.19, making the difference \$971.81. The amount to be paid on May 1, 1918, to satisfy this difference is found, by dividing \$971.81, by 1.00369863, the "amount" of \$1 for 45 days (May, 30; and June, 15), at 3% to be \$968.23 (\$968.228).

If, in the example given above, the fourth payment were made May 16, 1917, the taxpayer would be required to pay the whole of the difference, \$971.81, as no interest would be allowable on same under the law.

If the taxpayer elects to pay the whole of the tax in advance, that is, after the close of the taxable year and prior to the expiration of $4\frac{1}{2}$ months after the close of the taxable year, the amount to be paid to satisfy the tax will be determined by dividing the amount of said tax by 1.00 plus the interest on \$1 at 3% per annum (365 days) for the number of days from the date of payment to the date now fixed by law for such payment.

If the advance payment in whole is made at the time of filing the return, and if upon the examination of such return in this office, it is found that the payment was in excess of the amount required, together with the interest thereon to satisfy the tax actually due, the taxpayer will be entitled to the refund of the amount of excess payment (but not the interest thereon) by making claim for same on Form 46.

In arriving at the amount of excess payment, the tax assessed should be divided by 1.00 plus the interest at 3% per annum (365 days) on \$1 for the number of days from the date of payment to the date now fixed by law for such payment. The difference between the amount actually paid in advance and the quotient will be the amount of excess payment.

The interest at the rate of 3% per annum (365 days), allowed to a taxpayer on advance payments on income and excess profits taxes, must be considered income and accounted for as income by the taxpayer in his return for the year in which said interest is allowed. (T. D. 2622.)

INTEREST TABLE

Interest on \$1.00 at 3 per cent per 365 days, 1 day to 165 days.

Days	Interest	Days	Interest
1.....	\$.0000082192	48.....	.003945205
2.....	.000164384	49.....	.004027397
3.....	.000246575	50.....	.004109589
4.....	.000328767	51.....	.004191781
5.....	.000410959	52.....	.004273973
6.....	.000493151	53.....	.004356164
7.....	.000575342	54.....	.004438356
8.....	.000657534	55.....	.004520548
9.....	.000739726	56.....	.004602740
10.....	.000821918	57.....	.004684932
11.....	.000904110	58.....	.004767123
12.....	.000986301	59.....	.004849315
13.....	.001068493	60.....	.004931507
14.....	.001150685	61.....	.005013699
15.....	.001232877	62.....	.005095890
16.....	.001315068	63.....	.005178082
17.....	.001397260	64.....	.005260274
18.....	.001479452	65.....	.005342466
19.....	.001561644	66.....	.005424658
20.....	.001643836	67.....	.005506849
21.....	.001726027	68.....	.005589041
22.....	.001808219	69.....	.005671233
23.....	.001890411	70.....	.005753425
24.....	.001972603	71.....	.005835616
25.....	.002054795	72.....	.005917808
26.....	.002136986	73.....	.006000000
27.....	.002219178	74.....	.006082192
28.....	.002301370	75.....	.006164384
29.....	.002383562	76.....	.006246575
30.....	.002465753	77.....	.006328767
31.....	.002547945	78.....	.006410959
32.....	.002630137	79.....	.006493151
33.....	.002712329	80.....	.006575342
34.....	.002794521	81.....	.006657534
35.....	.002876712	82.....	.006739726
36.....	.002958904	83.....	.006821918
37.....	.003041096	84.....	.006904110
38.....	.003123288	85.....	.006986301
39.....	.003205479	86.....	.007068493
40.....	.003287671	87.....	.007150685
41.....	.003369863	88.....	.007232877
42.....	.003452055	89.....	.007315068
43.....	.003534247	90.....	.007397260
44.....	.003616438	91.....	.007479452
45.....	.003698630	92.....	.007561644
46.....	.003780822	93.....	.007643836
47.....	.003863014	94.....	.007726027

Days	Interest	Days	Interest
95.....	.007808219	131.....	.010767123
96.....	.007890411	132.....	.010849315
97.....	.007972603	133.....	.010931507
98.....	.008054795	134.....	.011013699
99.....	.008136986	135.....	.011095890
100.....	.008219178	136.....	.011178082
101.....	.008301370	137.....	.011260274
102.....	.008383562	138.....	.011342466
103.....	.008465753	139.....	.011424658
104.....	.008547945	140.....	.011506849
105.....	.008630137	141.....	.011589041
106.....	.008712329	142.....	.011671233
107.....	.008794521	143.....	.011753425
108.....	.008876712	144.....	.011835616
109.....	.008958904	145.....	.011917808
110.....	.009041096	146.....	.012000000
111.....	.009123288	147.....	.012082192
112.....	.009205479	148.....	.012164384
113.....	.009287671	149.....	.012246575
114.....	.009369863	150.....	.012328767
115.....	.009452055	151.....	.012410959
116.....	.009534247	152.....	.012493151
117.....	.009616438	153.....	.012575342
118.....	.009698630	154.....	.012657534
119.....	.009780822	155.....	.012739726
120.....	.009863014	156.....	.012821918
121.....	.009945205	157.....	.012904110
122.....	.010027397	158.....	.012986301
123.....	.010109589	159.....	.013068493
124.....	.010191781	160.....	.013150685
125.....	.010273973	161.....	.013232877
126.....	.010356164	162.....	.013315068
127.....	.010438356	163.....	.013397260
128.....	.010520548	164.....	.013479452
129.....	.010602740	165.....	.013561644
130.....	.010684932		

[Page 405.]

Excess Payment of Tax. An excess payment of tax in one year cannot be offset against an assessment of tax for a subsequent year. (Reg. 33 Rev., Art. 39.)

Manner of Payment of Taxes. The date on which the collector receives an uncertified check in payment of the tax is considered the date of payment, unless the check is returned dishonored. (T. D. 2627.) In the payment of the tax the fractional part of a cent is disregarded unless

it amounts to a half cent or more, in which case the fraction is increased to one cent. (Reg. 33 Rev., Art. 41.)

[Page 415.]

Waiving the Three-year Limitation. Where the limitation of the statute as to assessment has run and a written waiver of exemption from assessment is given by the taxpayer, the ad valorem penalty of 50 cent, addition to tax, is not to be assessed for delinquency in filing return. (Reg. 33 Rev., Art. 52.)

[Page 417.]

Lien for Unpaid Taxes. Tax due on income has the status of a debt due the United States. Persons receiving property charged with such indebtedness must answer for the debt. (Reg. 33 Rev., Art. 39.)

CHAPTER 37

PENALTIES AND COMPROMISES

[Page 421.]

Specific penalties provided by the income tax law in the case of individuals are held to attach to the person and in the case of the death of such person are non-enforceable. Ad valorem penalties (those measured by income) attach to the income and are to be enforced regardless of the death of the owner of the income by which the penalty is measured. (Reg. 33 Rev., Art. 51.)

[Page 422.]

Exception. The words "reasonable cause" as used in the provision of law referred to in R. S. Sec. 3176, as

amended by Act of September 8, 1916, is held to be such a condition of fact as had the taxpayer in default exercised ordinary business care and prudence it would have been impracticable or impossible for him to have filed his return in the prescribed time. Delinquent returns must be accompanied by an affirmative showing of fact alleged as reasonable cause for excuse from the 50 per cent penalty. This showing must be in the form of an affidavit, under oath, and should be attached to the return. (Reg. 33 Rev., Art. 54.)

[Page 424.]

Fraudulent Returns. The 100 per cent penalty is added to the amount of tax shown by the correct return. In addition a fine not exceeding \$2,000, or imprisonment not exceeding one year or both, in the discretion of the court, with costs of prosecution, is also imposed. (Reg. 33 Rev., Art. 53.)

[Page 425.]

Delay in Payment of the Tax. Collectors should issue Form 17 for the purpose of fixing definitely the date when the five per cent penalty accrues and interest at one per cent per month begins to run. (Reg. 33, Rev. Art. 41.) A specific penalty of not less than \$20 nor more than \$1,000 is also imposed for delay in paying the tax. (id. Art. 51.)

CHAPTER 40

INFORMATION AT THE SOURCE

[Page 450.]

Miscellaneous Income, Gains or Profits. It has been held in an informal ruling that such payments as are made
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for advertising, freight, cartage, fire insurance premiums, and discounts paid to banks are not required to be reported by the payor. (Telegram from Commissioner of Internal Revenue, dated February 5, 1918.) Where a person receives a cash compensation for services rendered and in addition thereto living quarters, the value to such person of the quarters furnished constitutes income subject to the tax and the return of information at the source required under Section 28 of the Act of October 3, 1917, must include the cash compensation received plus the value of the living quarters if the sum of both equals or exceeds \$800 for a tax year. (Reg. 33 Rev., Art. 34.)

[Page 454.]

Procedure in Paying Income. When the person receiving a payment falling within the provisions of law for information at the source is not the actual owner of the income received, the name and address of the actual owner shall be furnished upon demand of the person, corporation, partnership, or association paying the income, and in default of a compliance with such demand the payee becomes liable to a penalty of not less than \$20 nor more than \$1,000. (Reg. 33 Rev., Art. 36.) The law imposes no duty however upon the payor of the income to inquire as to the ownership thereof. It would seem that the payor of the income is fully protected by reporting in good faith the name and address of the one to whom the income is paid.

[Page 454.]

Return of Information at the Source. Two forms of return have been prescribed by the Treasury Department for reporting payments of miscellaneous income.

One form is known as Form 1099, a copy of which is required to be filled out for each person, firm or corporation to whom or which fixed or determinable gains, profits or income of \$800 or more has been paid during the tax year. The other (Form 1096) is merely a letter of transmittal to be used in forwarding the several Forms 1099 to the commissioner. (Reg. 33 Rev., Arts. 34 and 35.) No form has yet been issued for the purpose of reporting dividends. This return, when required, will be made upon a form prescribed for this purpose, and will be forwarded direct to the office of the Commissioner of Internal Revenue within ten days from the date of the receipt of the notice requiring such return. (id. Art. 237.) No form of return has yet been prescribed for use by brokers in reporting the gains and losses of their customers.

[Page 455.]

Collection of Foreign Payments. Persons, corporations or partnerships, undertaking as a matter of business or for profit the collection of foreign items are required to write or stamp on the face of each item: "Information obtained and furnished by..... (name of collecting agent)." (Reg. 33 Rev., Art. 48.)

CHAPTER 41

COLLECTION OF TAX AT THE SOURCE

[Page 457.]

An annual return of the tax withheld is required to be made in the manner and on the form, prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. This return is to be

made after February 1 and on or before March 1 annually. The return shows the name and address of the withholding agent, character of income, and the name and address of the recipient or his agent, amount of income, exemption claimed, and the amount of tax at 2 per cent withheld thereon. Any income withheld from a citizen or resident alien in 1917 prior to October 3, 1917, except in the case covered by section 9 (c) (from interest paid on securities having a tax-free covenant clause) of the act of September 8, 1916, as amended, shall be released by the withholding agent and paid over to the individual from whom it was withheld or his proper legal representative. The income upon which such tax was so deducted and released shall be included in the return, if any, of such individual for the purpose of assessment and collection of the income tax. (Reg. 33 Rev., Art. 47.) Where substitute certificate Form 1059 was used in 1917 in collecting coupons from bonds, and the amount withheld is required to be released and paid back under the provisions of Section 1212 of the Act of October 3, 1917, the withholding agent should request the bank or collection agency using such certificate to disclose the name and address of the owner of the bond, as shown by the original certificate, and the bank or collection agency is required to make such disclosure to the withholding agent. If the owner of the bond was a citizen or resident of the United States, the withholding agent should refund the amount of tax deducted. If the owner was a non-resident alien no refund should be made, but the withholding agent should report the amount accordingly and pay over the sum as in other cases where withholding took place against non-resident aliens. (T. D. 2635.)

[Page 465.]

Withholding on Payment of Bond Interest. Where no ownership certificate accompanies a coupon and it is impossible to ascertain the information necessary to determine whether or not the tax should be withheld or the rate which applies, the tax should be withheld at the rate of 6%. If any excess amount of tax should thus be paid to the Government, the payment may be adjusted by claim for refund. If coupons are not accompanied by certificates disclosing ownership, the first bank which accepts the coupon for collection is required to fill out Form 1000 as revised January, 1918, entering the interest on line 4 and the debtor corporation will be required to withhold the tax on that amount. (Telegram from the Treasury Department dated January 28, 1918, and letter from Treasury Department dated January 30, 1918; I. T. S., 1918, Paragraphs 3071 and 3072.)

[Page 466.]

Interest on Bonds Containing Covenants to Pay the Tax. The withholding provisions of the income tax law apply in the case of citizens and resident aliens only in case income is derived from interest on bonds and mortgages, deeds of trust, or other similar obligations of corporations, associations, etc., which have a "tax-free" covenant clause (i. e., a contract or provision by which the obligor agrees to pay any portion of the tax imposed by this title upon the obligee or to reimburse the obligee in any portion of the tax or to pay the interest without deduction for any tax which the obligor may be required or permitted to pay thereon or to retain therefrom under any law of the United States), regardless of the amount and period of payment. The amount to be withheld is 2 per cent on the amount of payment, un-

less the person entitled to receive such interest shall file with the withholding agent, on or before February 1, a signed notice in writing claiming the benefit of an allowable exemption under section 7, act of September 8, 1916, as amended. (Reg. 33 Rev., Art. 43.) Confusion seems to have been created in the minds of bondholders as to the meaning of that provision of the law which refers to the filing of a claim for exemption on or before February 1st. No such claim should be filed if a bondholder intends to have the corporation assume the burden of 2 per cent normal tax on the interest paid to him. If it is desired to file a claim for exemption the same may be filed on or before February 1st of the year following that in which the interest was received. In filing such claim for exemption Form 1001 should be used. The total amount of exemption which may be claimed is the personal exemption allowed by the Act of October 3, 1917, that is, \$1,000 in the case of unmarried persons, and \$2,000 in the case of married persons and heads of families, with an additional \$200 for each minor child. (See Reg. 33 Rev., Art. 44.) The matter of complying with the covenant of the bond is a matter to be adjusted between the debtor corporation and the bondholder. If, however, it is clearly established by affidavit or otherwise that the debtor corporation has actually withheld and paid to the proper officers of the United States the tax on such interest income, the recipient, having returned such interest as income, may take credit against any tax to which subject on the basis of return, for the tax so paid by the debtor corporation. (Reg. 33 Rev., Art. 122.)

[Page 468.]

Car-trust Certificates. Car-trust certificates are held to be obligations similar to corporate bonds and

mortgages. The trustees are therefore required to withhold the tax and if the certificates contain a contract or provision by which the obligor agrees to pay any portion of the tax imposed by this title upon the obligee or reimburse the obligee for any portion of the tax, or to pay the interest without deduction for any tax which the obligor may be required to pay, the trustees in such cases, in making interest payments on these certificates, will, in the absence of claims for exemption when interest payments are made to individuals, withhold the normal income tax on such payments regardless of the amount thereof. (Reg. 33 Rev., Art. 188.)

[Page 471.]

Ownership Certificates. The owners of bonds of domestic and resident corporations shall, when presenting interest coupons for payment, file a certificate of ownership for each issue of bonds, showing the name and address of the debtor corporation, the name and address of the owner of the bonds, whether the payee is married or the head of a family, and the amount of interest. (Reg. 33 Rev., Art. 43.)

[Page 473.]

Form 1000. Form 1000, revised, shall be used (a) when no personal exemption is claimed against interest on bonds containing a "tax-free" covenant by citizens or residents of the United States; (b) by nonresident alien individuals, foreign corporations having no office or place of business in the United States whether or not such bonds contain a "tax-free" covenant; and (c) in the case where coupons are received not accompanied by certificates of ownership. The first bank receiving coupons not accompanied by ownership certificates will

make a certificate crossing out "owner" and inserting "payee" and will enter the amount of interest on line 4. (Reg. 33 Rev., Art. 43.)

[Page 473.]

Form 1001. Form 1001, revised, shall be used (a) when personal exemption is claimed against interest on bonds containing a "tax-free" covenant by citizens or residents of the United States, also when presenting coupons from bonds not containing a "tax-free" covenant; (b) by domestic partnerships, corporations, or associations; (c) by nonresident alien partnerships; and (d) by foreign corporations having an office or place of business in the United States, whether or not such bonds contain a "tax-free" covenant. In case a citizen or resident individual receives interest on bonds containing a "tax-free" covenant in excess of the amount of personal exemption which the individual may claim, any such excess must be reported on Form 1000, revised. (Reg. 33 Rev., Art. 43.)

[Page 473.]

Form 1004. This form is superseded by revised Form 1000 referred to above.

[Page 473.]

Substitute Certificates. Collecting agents, responsible banks and bankers receiving coupons for collection with ownership certificates attached may present the coupons with the original certificates to the debtor corporation or its duly authorized withholding agent for collection or the original certificates may be detached and forwarded direct to the Commissioner of Internal Revenue, provided such collecting agent shall substitute for such

certificate its own certificate and shall keep a complete record of each transaction showing—

1. Serial number of item received.
2. Date received.
3. Name and address of person from whom received.
4. Name of debtor corporation.
5. Class of bonds from which coupons were cut.
6. Face amount of coupons.

For the purpose of identification the substitute certificates shall be numbered consecutively and corresponding numbers given the original certificates of ownership. Substitute certificates by collecting agents, banks and bankers, in lieu of original certificates of ownership accompanying coupons presented for collection shall be discontinued with respect to ownership certificates presented with coupons for collection by non-resident alien individuals, firms, corporations, organizations, etc. In all such cases the original certificates of ownership shall be forwarded to the debtor corporation without substitution. The debtor corporation or its duly authorized withholding agent shall forward all certificates to the Collector of Internal Revenue with its duplicate monthly list returned, Form 1012, revised, and such collector shall forward the original return and the certificates to the commissioner, as heretofore. (Reg. 33 Rev., Art. 43.)

[Page 476.]

Banks. The long-established rule that banks were not required to withhold the normal tax on interest paid or accruing on deposits has been revoked and banks are now required to withhold a normal tax of 2 per cent on interest paid to non-resident alien individuals. (T. D. 2652.) It seems the word "paid" used in the foregoing ruling is intended to include interest which is actually

paid to non-resident alien individuals and also interest credited to their accounts, that is, deduction is to take place when the interest is placed at the disposal of the depositors.

[Page 477.]

Employers. It is held that salaries, wages and commissions, paid by domestic corporations, resident individuals, or partnerships to non-resident alien employees for services rendered entirely in a foreign country are not subject to deduction and withholding of the normal tax, and such payments of income will not be subject to the income tax in the hands of the recipient as from a source within the United States. (Reg. 33 Rev., Art. 32.)

[Page 477.]

Lessors. Rent paid by domestic corporations, resident individuals, or partnerships to non-resident aliens as rent for property located in a foreign country is not subject to collection at the source. (Reg. 33 Rev., Art. 32.)

[Page 479.]

Monthly List Returns. The tax withheld from bond interest will be accounted for monthly on Income-Tax Form 1012 (Revised 1918).

[Page 480.]

Annual List Returns. Return is to be made for the tax withheld in manner and on a form to be prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. This return is to be made after February 1 and on or before March 1 annually. The return shall show the name and address

of the withholding agent, character of income, and the name and address of the recipient or his agent, amount of income, exemption claimed, and the amount of tax at 2 per cent withheld thereon. (Reg. 33, Rev. Art. 46.) The form prescribed as an annual list return for reporting the normal tax withheld on salaries, wages, rent, etc., paid to non-resident alien individuals is Form 1042 (Revised 1918). Separate reports of the payments entered on such form are also required to be made on Form 1098. The form to be used in reporting annually income withheld at the source on payments of interest on corporate bonds and dividends on corporate stock is Form 1013 (Revised 1918).

CHAPTER 44

TAX ON UNDISTRIBUTED INCOME OF CORPORATIONS

[Page 496.]

Undistributed Net Income. In order to determine the amount of such net income subject to this tax, the increase in the surplus balance at the close of the taxable year as compared with the surplus balance at the beginning of such year, shall be analyzed so to account for the disposition thereof in increase in assets, decrease in liabilities or in dividends, and the net increase in current assets over current liabilities shall be subject to the above tax of 10 per cent unless it can be conclusively shown by the corporation that such increase is retained to provide for an actual increase in business or for additions to plant or the reduction of bonded or other fixed liabilities. (Reg. 33, Rev. Art. 238.)

CHAPTER 45¹

THE WAR EXCESS PROFITS TAX

DEFINITIONS

Article 1. Definitions.—When used in these regulations the terms defined in Articles 2 to 9, inclusive, shall unless otherwise indicated by the context, be deemed to be used only with the scope or meaning ascribed to them respectively in such articles.

Art. 2. Corporation.—The term “corporation” includes joint-stock companies or associations, no matter how created or organized, insurance companies and limited partnerships.²

Art. 3. Domestic and foreign.—The term “domestic” means created under the law (statutory or other) of the United States or any State thereof, Alaska, Hawaii, or the District of Columbia, and the term “foreign”

¹ The most practical discussion of the War Excess Profits Tax Law at the present time is contained in the official regulations of the Treasury Department, the text of which is printed in full herein with the author's comments and explanation in the footnotes. These regulations are officially designated “Regulations No. 41.”

² See Holmes Income Tax, Ch. 12, pp. 126 and 127; also Ch. 10, p. 103. The law defines the term “corporation” to include joint-stock companies or associations and insurance companies. To include all limited partnerships in the term seems to extend the provision of the statute by implication beyond the clear import of the language used, contrary to the established rules of construction. Limited partnerships or partnership associations formed under some statutes may have characteristics more in the nature of a joint-stock company than a partnership but this is not true of all limited partnerships. The status of a limited partnership should rather be determined in each instance according to the similarity of its characteristics to those of a joint-stock association.

means created under the law (statutory or other) of any other possession of the United States or of any foreign country or government.

Art. 4. United States.—The term “United States” (when used in a geographical sense) means only the States thereof, Alaska, Hawaii, and the District of Columbia.

Art. 5. Taxable year.—The term “taxable year” means the 12 months ending December 31 of each year, except in the case of a corporation or partnership which has fixed its own fiscal year, in which case it means such fiscal year. The first taxable year is the year ending December 31, 1917, except that in the case of a corporation or partnership which has fixed its own fiscal year, the first taxable year is the fiscal year ending during the calendar year 1917.³

Art. 6. Prewar period.—The term “prewar period” means the calendar years 1911, 1912, and 1913, or if a corporation or partnership was not in existence or an individual was not engaged in the trade or business during the whole of such three years, then as many of such years during the whole of which the corporation or partnership was in existence or the individual was engaged in the trade or business.

Art. 7. “Trade,” “business,” “trade or business” in case of corporations and partnerships.—In the case of a *corporation or partnership* all income from whatever source derived is deemed to be received from its trade or business, and the terms “trade,” “business,” and “trade or business” include all sources of income.

Art. 8. “Trade” in the case of individuals.—In the

³ For special provisions as to prorating the amount of tax due for the portion of any fiscal year ending during the calendar year 1917, see Articles 19 and 20.

case of an *individual*, the terms "trade," "business," and "trade or business" comprehend all his activities for gain, profit, or livelihood, entered into with sufficient frequency, or occupying such portion of his time or attention as to constitute a vocation, including occupations or professions. When such activities constitute a vocation they shall be construed to be a trade or business whether continuously carried on during the taxable year or not, and all the income arising therefrom shall be included in his return for excess-profits tax.

In the following cases the gain or income is not subject to excess-profits tax, and the capital from which such gain or income is derived shall not be included in "invested capital:" (a) Gains or profits from transactions entered into for profit, but which are isolated, incidental, or so infrequent as not to constitute an occupation, and (b) the income from property arising merely from its ownership, including interest, rent, and similar income from investments except in those cases in which the management of such investments really constitutes a trade or business.

Art. 9. "Dividend."—The term "dividend" has the same meaning as in Sec. 31 of the act of September 8, 1916, as amended by the act of October 3, 1917.⁴

CORPORATIONS, PARTNERSHIPS, AND INDIVIDUALS SUBJECT TO THE TAX

Art. 10. Corporations.—Every domestic corporation which has for the taxable year a net income of \$3,000 or more, is unless exempt under Art. 13, required to make a return and pay the tax, if any.⁵

⁴ See Holmes Income Tax, Ch. 23, p. 262.

⁵ There is no express provision in the statute requiring cor-

Every foreign corporation which has for the taxable year a net income of \$3,000 or more from sources within the United States is, unless exempt under Art. 13, required to make a return and to pay the tax, if any.

Art. 11. Partnerships.—Every domestic partnership which has for the taxable year a net income of \$6,000 or more is, unless exempt under Art. 13, required to make a return and to pay the tax, if any.

Every foreign partnership which has for the taxable year a net income of \$3,000 or more from sources within the United States is, unless exempt under Art. 13, required to make a return and to pay the tax, if any.

Art. 12. Individuals.—Every citizen or resident of the United States who has for the taxable year an aggregate net income in excess of \$6,000 from trades, businesses, occupations or professions is, unless exempt under Art. 13, required to make a return and to pay the tax, if any.⁵

Every nonresident alien individual who has for the taxable year an aggregate net income of \$3,000 or more from trades, businesses, occupations, or professions carried on within the United States is, unless exempt under Art. 13, required to make a return and to pay the tax, if any.

Art. 13. Exemptions.—The following are exempt from the tax:

(a) Corporations exempt under the provisions of Sec.

porations or individuals to make returns separate from their returns of annual net income for the purpose of this tax, but under Sec. 213 of the act the Commissioner of Internal Revenue is given the authority on which this ruling is based. The time for filing excess profits tax returns has been extended to April 1, 1918. (T. D. 2650). As to corporations dissolved prior to the passage of the law. See p. 674.

11 of Title I of the act of September 8, 1916, from the tax imposed by such title.⁶

(b) Partnerships carrying on or doing the same kind of business or coming within the same description.

(c) Individuals to the extent that they carry on or do the same kind of business or come within the same description.

RATES AND COMPUTATION OF TAX

Art. 14. Classification of net income.—For the purposes of the excess profits tax net income which is subject to the tax shall be divided into two classes, as follows:

A. Net income which is derived from a trade or business having no invested capital, or not more than a nominal capital, including in the case of an *individual* salaries, wages, fees, or other compensations; and

B. Net income which is derived from a trade or business having invested capital.

In the case of a *corporation or partnership*, all the trades and businesses in which it is engaged will be treated as a single trade or business,⁷ and its entire income will be held to be of the same class as the income from its principal trade or business.

In the case of an *individual* the net income subject to the excess profits tax shall be classified as provided in this Article. Net income of class A shall be taxed as provided in Art. 15, and net income of class B shall be taxed as provided in Art. 16.

Art. 15. Rate of tax on income of class A.—The tax upon net income of class A as defined in Art. 14 shall be

⁶ See Holmes Income Tax, Ch. 15, p. 193.

⁷ See Sec. 201 of the Law.

computed at the rate of 8 per cent upon the amount thereof in excess of \$3,000 in the case of a *domestic corporation*; upon the amount thereof in excess of \$6,000 in the case of a *domestic partnership* or of a *citizen* or *resident* of the United States; and upon the whole thereof in the case of a *foreign corporation or partnership* or of a *non-resident alien individual*.

Art. 16. Rate of tax on income of class B.—The tax upon net income of class B as defined in Art. 14 shall, except as otherwise provided in Art. 17, be computed at the following rates:

20 per cent of the amount of the net income in excess of the deduction (determined as provided in Articles 21, 23, and 24) and not in excess of 15 per cent of the invested capital for the taxable year;

25 per cent of the amount of the net income in excess of 15 per cent and not in excess of 20 per cent of such capital;

35 per cent of the amount of the net income in excess of 20 per cent and not in excess of 25 per cent of such capital;

45 per cent of the amount of the net income in excess of 25 per cent and not in excess of 33 per cent of such capital;

60 per cent of the amount of the net income in excess of 33 per cent of such capital.

Illustrations.—(1) A corporation has a capital of \$100,000, prewar earnings of 7 per cent, and a net income for the taxable year of \$75,000.

The deduction allowed will be 7 per cent of the capital, or \$7,000, plus \$3,000 specific deduction, a total of \$10,000.

The amount of the net income taxable at each rate will be as follows:

In excess of the deduction and not in excess of 15 per cent of the capital (rate, 20 per cent)	\$5,000
In excess of 15 per cent of the capital and not in excess of 20 per cent thereof (rate, 25 per cent)	5,000
In excess of 20 per cent of the capital and not in excess of 25 per cent thereof (rate, 35 per cent)	5,000
In excess of 25 per cent of the capital and not in excess of 33 per cent thereof (rate, 45 per cent)	8,000
In excess of 33 per cent of the capital (rate, 60 per cent)	42,000
The tax would then be computed as follows:	

20 per cent of \$5,000	\$ 1,000
25 per cent of 5,000	1,250
35 per cent of 5,000	1,750
45 per cent of 8,000	3,600
60 per cent of 42,000	25,200
Total tax	\$32,800

(2) An individual or partnership has a capital of \$100,000, prewar earnings of 8 per cent, and a net income for the taxable year of \$22,500.

The deduction allowed will be 8 per cent of the capital, or \$8,000, plus \$6,000 specific deduction, a total of \$14,000.

The amount of the net income taxable at each rate will be as follows:

In excess of the deduction and not in excess of 15 per cent of the capital (rate, 20 per cent)	\$1,000
In excess of 15 per cent of the capital and not in excess of 20 per cent thereof (rate, 25 per cent)	5,000
In excess of 20 per cent of the capital and not in excess of 25 per cent thereof (rate, 35 per cent)	2,500

The tax would then be computed as follows:

20 per cent of \$1,000.....	\$ 200
25 per cent of 5,000.....	1,250
35 per cent of 2,500.....	875
Total tax	\$2,325

Art. 17. When deduction exceeds 15 per cent of invested capital.—In any case in which the deduction determined as provided in articles 21, 23 and 24 is greater than 15 per cent of the invested capital and therefore can not be fully allowed under the first rate or bracket of Art. 16, then any remaining portion of the deduction will be allowed under the second bracket, and continued if necessary into the succeeding bracket or brackets until the entire amount of the deduction is allowed.

Illustrations.—(1) A corporation has a capital of \$9,000; prewar earnings of 9 per cent; and a net income for the taxable year of \$10,000.

The deduction allowed will be 9 per cent of the capital, or \$810, plus \$3,000 specific deduction, a total of \$3,810.

The amount of the net income in each bracket will be as follows:

15 per cent of the capital.....	\$1,350
In excess of 15 per cent of the capital and not in excess of 20 per cent thereof.....	450
In excess of 20 per cent of the capital and not in excess of 25 per cent thereof.....	450
In excess of 25 per cent of the capital and not in excess of 33 per cent thereof.....	720
In excess of 33 per cent of the capital.....	7,030

It is evident that the total deduction of \$3,810 is greater than 15 per cent of the capital and so is not fully

absorbed by the amount of net income not in excess of 15 per cent of the capital. In such case, applying Art. 17, the total deduction of \$3,810 will be distributed as follows:

\$1,350 in the first bracket, leaving nothing to be taxed at the 20 per cent rate.

\$450 in the second bracket, leaving nothing to be taxed at 25 per cent rate.

\$450 in the third bracket, leaving nothing to be taxed at the 35 per cent rate.

\$720 in the fourth bracket, leaving nothing to be taxed at the 45 per cent rate.

There still remains \$840 of the deduction to be allowed in the fifth bracket against the \$7,030 of income which would otherwise be taxable under that bracket. There would then be \$6,190 of net income left to be taxed at 60 per cent rate under the fifth bracket. Hence, the total excess-profits tax in this case would be \$3,714.

(2) An individual or partnership has a capital of \$40,000, prewar earnings of 9 per cent, and a net income for the taxable year of \$12,000.

The deduction allowed will be 9 per cent of the capital, or \$3,600, plus \$6,000 specific deduction, a total of \$9,600.

The amount of the net income in each bracket will be as follows:

15 per cent of the capital.....	\$6,000
In excess of 15 per cent of the capital and not in excess of 20 per cent thereof.....	2,000
In excess of 20 per cent of the capital and not in excess of 25 per cent thereof.....	2,000
In excess of 25 per cent of the capital and not in excess of 33 per cent thereof.....	2,000

It is evident that the total deduction of \$9,600 is greater than 15 per cent of the capital and so is not fully absorbed by the amount of net income not in excess of 15 per cent of the capital. In such case, applying Art. 17, the total deduction of \$9,600 will be distributed as follows:

\$6,000 in the first bracket, leaving nothing to be taxed at the 20 per cent rate.

\$2,000 in the second bracket, leaving nothing to be taxed at the 25 per cent rate.

\$1,600, the balance of the deduction, to be allowed against the \$2,000 of income in the third bracket.

There would then be \$400 of income left in the third bracket to be taxed at the 35 per cent rate, and \$2,000 in the fourth bracket to be taxed at the 45 per cent rate. Hence, the total excess-profits tax in this case would be \$1,040.

Art. 18. Constructive capital for application of rates.

—Where the deduction allowed to a taxpayer is determined under Art. 24, the invested capital for the purpose of applying the rates of taxation under Art. 16 shall be deemed to be an amount which bears the same ratio to the net income of the trade or business for the taxable year which the average invested capital for the corresponding calendar year of representative corporations, partnerships, and individuals engaged in a like or similar trade or business bears to their average net income.

The Commissioner of Internal Revenue in determining for any calendar year the ratio which the average invested capital of representative corporations, partnerships, and individuals engaged in any particular trade or business bears to their average net income, will in-

clude the invested capital and net income of representative corporations and partnerships for fiscal years ending during such calendar year.

For the purpose of applying this article in the case of a corporation or partnership which has fixed its own fiscal year, the ratio determined for the calendar year ending during such fiscal year shall be used.

Art. 19.—Computation of tax for fiscal year, part of which falls within calendar year 1916.—If a *corporation or partnership* prior to March 1, 1918, makes a return for a fiscal year, part of which falls within the calendar year 1916, the tax for the first taxable year shall be that proportion of the tax computed upon the net income for such fiscal year which the number of months from January 1, 1917, to the end of such fiscal year bears to the entire number of months in such fiscal year.

Art. 20. Computation of tax for period of less than 12 months.—If a *corporation or partnership* at any time, either because it has just designated a fiscal year as provided in Sections 8 or 13 of the act of September 8, 1916⁸ or for any other reason, makes a return for a period of less than 12 months, the deduction will be an amount which bears the same ratio to the deduction allowable for a full year as the number of months in such period bears to 12 months.

COMPUTATION OF THE DEDUCTION

Art. 21. Trade or business having invested capital.—The deduction used in computing the rates of tax under Art. 16 shall, except in cases coming within the conditions specified in Articles 23 and 24, be as follows:

⁸ See Holmes Income Tax, Ch. 12, p. 153.

(a) In the case of a *domestic corporation* the sum of (1) an amount equal to the same percentage of the invested capital for the taxable year which the average amount of the annual net income of the trade or business during the prewar period was of the invested capital for the prewar period (except that 7 per cent shall be used if such percentage was less than 7 per cent, and 9 per cent shall be used, if such percentage was more than 9 per cent, and 8 per cent shall be used if the corporation was not in existence during the whole of at least one calendar year during the prewar period⁹), and (2) \$3,000.

(b) In the case of a *domestic partnership* or of a *citizen or resident* of the United States, the sum of (1) an amount equal to the same percentage of the invested capital for the taxable year which the average amount of the annual net income of the trade or business during the prewar period was of the invested capital for the prewar period (except that 7 per cent shall be used if such percentage was less than 7 per cent, and 9 per cent shall be used if such percentage was more than 9 per cent, and 8 per cent shall be used if the partnership was not in existence or the individual was not engaged in the trade or business during the whole of at least one calendar year during the prewar period,⁹) and (2) \$6,000.

(c) In the case of a *foreign corporation or partnership* or of a *non-resident alien individual*, an amount equal to the same percentage of the invested capital for the taxable year which the average amount of the annual net income of the trade or business during the prewar period was of the invested capital for the prewar period (except that 7 per cent shall be used if such percentage was less than 7 per cent, and 9 per cent shall be used if

⁹ Except in the cases covered by Art. 22.

such percentage was more than 9 per cent; and 8 per cent shall be used if the corporation or partnership was not in existence or the individual was not engaged in the trade or business during the whole of at least one calendar year during the prewar period ⁹).

Art. 22. Trade or business reorganized on or after January 2, 1913.—If a trade or business carried on by a *corporation, partnership or individual* was formally organized or reorganized on or after January 2, 1913, but is substantially a continuation of a trade or business carried on prior to that date, then the corporation or partnership shall be deemed to have been in existence, or the individual shall be deemed to have been engaged in the trade or business, prior to that date, and for the purpose of computing the deduction the net income and invested capital of the predecessor shall be deemed to have been the net income and invested capital of the present owner for the prewar period.¹⁰

Art. 23. When income for prewar period cannot be satisfactorily determined, or when net income was low during prewar period, or when there was no net income during prewar period.—In the following cases the deduction shall be determined as provided in this article:

(a) If the Secretary of the Treasury is unable satisfactorily to determine the average amount of annual net income of the trade or business for the prewar period;

(b) If the Secretary of the Treasury upon complaint finds that during the prewar period the percentage of the net income to the invested capital of the taxpayer was lower by 1 per cent or more ¹¹ than the percentage of

¹⁰ The invested capital of the predecessor has no bearing on the invested capital for the taxable year. See Art. 49.

¹¹ The Law says "was low as compared with." It is doubtful if relief can be withheld under the law in cases where the vari-

the net income to the invested capital of representative corporations, partnerships or individuals engaged in a like or similar trade or business during the same period; or

(c) If, in the case only of a *domestic corporation or partnership* which was in existence during the prewar period, or of a *citizen or resident*¹² of the United States who was engaged in the trade or business during the prewar period, the Secretary of the Treasury upon complaint finds that during the prewar period there was no net income from the trade or business.

In such cases the deduction shall be—

(1) An amount equal to the same percentage of the invested capital for the taxable year which the average deduction (determined in the same manner as provided in Art. 21, without including the \$3,000 or \$6,000 therein referred to) for such year of representative corporations, partnerships, or individuals engaged in a like or similar trade or business, is of their average invested capital for such year, plus¹³

(2) In the case of a *domestic corporation*, \$3,000, and
ation is less than 1%, and this ruling might be modified in exceptional cases.

¹² So limited by the language of the statute. This provision has particular application to development companies and to mining companies and similar enterprises requiring a long period of development before the stage of production is reached.

¹³ To illustrate: if the average deduction of coal mining concerns in the same vicinity and operating under substantially the same conditons of transportation and marketing is 9% for the taxable year, the same rate would be allowed to a mining concern which during the prewar period was, for instance, engaged in developing its property and had no net income or had not reached the point of full production and, therefore, had an income "low as compared with" other representative mining concerns at that time.

in the case of a *domestic partnership or a citizen or resident* of the United States, \$6,000.

In cases arising under subdivision (a) or (c) of this article the tax shall be assessed in the first instance upon the basis of a deduction computed by the use of 7 per cent. In cases arising under subdivision (b) the tax shall be assessed in the first instance upon the basis of a deduction determined as provided in Art. 21.

In any case under this article a taxpayer claiming the benefit of this provision shall at the time of making the return file a claim for abatement (Form 47) of the amount by which the tax so assessed exceeds a tax computed upon the basis of the deduction determined as provided in this article. In cases coming within the provisions of this article payment of that portion of the tax covered by the claim for abatement will not be required until the claim is decided. If, however, in the judgment of the Commissioner or Internal Revenue the interests of the United States would be jeopardized thereby, the right is reserved to require the claimant to give a bond of such amount and with such sureties as the commissioner thinks wise to safeguard such interests. The bond shall be conditioned for the payment of any tax found to be due with interest thereon, and if a bond satisfactory to the commissioner is not given within such time as he prescribes, the full amount of the tax assessed will become immediately due and the amount overpaid, if any, will upon final decision of the application, be refunded as a tax erroneously or illegally collected.

Art. 24. When invested capital cannot be satisfactorily determined.—If the Secretary of the Treasury is unable satisfactorily to determine the invested capital, the deduction shall be the sum of—

- (1) An amount equal to the same proportion of the

net income of the trade or business for the taxable year as the average deduction (determined in the same manner as provided in Art. 21 without including the \$3,000 or \$6,000 therein referred to) for the corresponding calendar year, or representative corporations, partnerships, and individuals engaged in a like or similar trade or business, is of their average net income, plus

(2) In the case of a *domestic corporation* \$3,000, and in the case of a *domestic partnership* or a *citizen or resident* of the United States, \$6,000.¹⁴

The Commissioner of Internal Revenue in determining for any calendar year the proportion which the average deduction of representative corporations, partnerships, and individuals engaged in any particular trade or business is of their average net income, will include the deductions and net income of representative corporations and partnerships for fiscal years ending during such calendar year.

For the purpose of applying this article in the case of a corporation or partnership which has fixed its own

¹⁴ See Sec. 210 of the Law. This provision relieves the taxpayer who through faulty accounting methods is unable to ascertain the amount of invested capital in the business. Wide latitude is given to the Secretary of the Treasury in the use of this method. In a trade in which there are many operators who do not keep books according to the recognized systems of accounting, the average return on invested capital may be ascertained among the representative concerns and also the ratio of deduction to income, which may thereupon be applied to all others in that industry whose invested capital cannot be satisfactorily determined. Thus, if the average return on invested capital is found to be 20% and the average deduction is found to be 25% of the net income for that taxable year, one whose income was \$36,000 would be entitled to a deduction of \$9,000—and the average return on invested capital being 20%, his “invested capital” would be arbitrarily fixed at \$180,000. See Art. 18.

fiscal year, the proportion determined for the calendar year ending during such fiscal year shall be used.

In every case or a trade or business having invested capital a return shall be made in the first instance in accordance with Art. 21 or 23, but the taxpayer may submit therewith a statement of reasons why in his opinion the tax should be assessed in accordance with this article.

NET INCOME—GENERAL PROVISIONS

Art. 25. Exemptions.—The following classes of income are exempt from the tax:

(a) Income exempt from taxation under Sec. 4 of the act of September 8, 1916, as amended.¹⁵

(b) Income derived from the business of life, health, and accident insurance combined in one policy issued on a weekly premium payment plan.

(c) Compensation or fees received by officers and employees under the United States or any State, Territory, or the District of Columbia for their services as such.¹⁶

Art. 26. Net income of foreign corporations, partnerships, and non-resident alien individuals.—In the case of a *foreign corporation or partnership* or a *non-resident alien individual* the net income shall be the net income from sources within the United States.

Art. 27. Dividends received from a foreign corporation which is subject to Federal income tax.—In the case of income derived by a *corporation or partnership* from dividends upon the stock of a foreign corporation, part of whose net income is subject to the income tax, there shall be deducted only that proportion of the divi-

¹⁵ See Holmes Income Tax, Ch. 16, p. 226.

¹⁶ Salaries of Congressmen have been held not to be exempt under this provision, on the ground that Congressmen are neither officers nor employees of the United States.

dends received upon such stock which the net income of such foreign corporation from sources within the United States is of its entire net income.¹⁷

Where dividends upon the stock of a foreign corporation are received by an *individual*, as a part of his income from trade or business, there shall be included in the net income that proportion of the dividends received upon such stock which the net income of such corporation from sources outside the United States is of its entire net income.

NET INCOME—CORPORATIONS

Art. 28. Taxable year.—The net income of a *corporation* for the taxable year shall be determined by adding (1) the amount of net income ascertained and returned for income tax purposes for such taxable year as provided in Title I of the act of September 8, 1916, as amended and (2) the amount, if any, received as interest on bonds or other obligations of the United States, issued after September 24, 1917 (other than the interest received on an amount of such bonds or obligations the aggregate principal of which does not exceed \$5,000),¹⁸ and deducting from the total so obtained the amounts received during the taxable year as dividends upon the stock or from the net earnings of other corporations, joint-stock companies or associations, or insurance companies, subject to the income tax imposed by Title I of such act of September 8, 1916, as amended, except as otherwise provided in Art. 27.¹⁹

¹⁷ See Holmes Income Tax, Ch. 23, p. 264.

¹⁸ See Holmes Income Tax, Ch. 22, p. 256.

¹⁹ Dividends may be deducted if the corporation from which they were received is subject to the income tax whether or not it is subject to the excess profits tax and whether or not the

Art. 29. Prewar period.—The net income of a *corporation* for the prewar period shall be computed as follows:

(a) For the calendar year 1911 by adding (1) the amount of net income shown in item 9 of the return made under Sec. 38 of the act of August 5, 1909, for the calendar year 1911, and (2) the amount of taxes paid to the United States *within* the calendar year 1911 under Sec. 38 of such act;²⁰

(b) For the calendar year 1912 by adding (1) the amount of net income shown in item 9 of the return made under Sec. 38 of the act of August 5, 1909, for the calendar year 1912, and (2) the amount of taxes paid to the United States *within* the calendar year 1912 under Sec. 38 of such act; and

(c) For the calendar year 1913 by adding (1) the amount of the entire net income shown in item 8 of the return made under Sec. II of the act of October 3, 1913, for the calendar year 1913, and (2) the amount of taxes paid *within* the calendar year 1913 under Sec. 38 of the act of August 5, 1909, and Sec. II or IV of the act of October 3, 1913, and deducting from the total so obtained the amounts received during the calendar year 1913 as dividends upon the stock or from the net earnings of other corporations, joint stock companies or associations,

dividends are from earnings of the year 1917 or from preceding years. Dividends from foreign corporations may be deducted if, and to the extent that the foreign corporation is subject to the income tax. See Art. 27.

²⁰ Under the 1909 and 1913 Laws corporations were permitted to deduct the amount of such taxes paid to the United States. Under the present laws income taxes cannot be deducted. Hence, for the purpose of comparing the average income for the prewar period with the income for the taxable year, the amount of such taxes are restored to the income account of the prewar years.

or insurance companies, subject to the income tax imposed by Sec. II of the act of October 3, 1913.

NET INCOME—PARTNERSHIPS

Art. 30. Taxable year.—The net income of a *partnership* for the taxable year shall be determined by adding the amount of its entire net income (or in the case of a foreign partnership, its entire net income from sources within the United States) ascertained upon the same basis and in the same manner as provided with respect to individuals for income-tax purposes by Title I of the act of September 8, 1916, as amended,²¹ including the amounts, if any, received during the year as interest on bonds or other obligations of the United States issued after September 24, 1917 (other than the interest on an amount of such bonds or obligations, the aggregate principal of which does not exceed \$5,000), and deducting therefrom—

(1) The amounts received during the taxable year as dividends upon the stock or from the net earnings of corporations, joint-stock companies or associations, or insurance companies, subject to the income tax imposed by Title I of the act of September 8, 1916, as amended, except as otherwise provided in Art. 27; and

(2) The deductions, if any, for salaries or interest allowed by Articles 32 and 33, if such deductions have not already been made.

Art. 31. Prewar period.—The net income of a *partnership* for each of the calendar years 1911, 1912, and 1913 shall be determined in the same manner as the net income for the taxable year, except that dividends upon the stock or from the net earnings of corporations, joint

²¹ See Holmes Income Tax, Ch. 4 and Ch. 5.

stock companies or associations, or insurance companies, subject to the tax imposed by Sec. 38 of the act of August 5, 1909, or by Sec. II of the act of October 3, 1913, shall be deducted.²²

Art. 32. Deductions allowed for salaries paid to partners.—In computing net income for purposes of the excess profits tax a *partnership* will be allowed to deduct as an expense reasonable salaries or compensation paid to individual partners for personal services actually rendered during the taxable year, if the payments are made in accordance with prior agreements and are properly recorded on the books of the partnership. In no case shall the salaries or compensation so deducted be in excess of the salaries or compensation customarily paid for similar services under like responsibilities by corporations engaged in like or similar trades or businesses.

With respect to any period prior to March 1, 1918, regardless of whether a previous agreement has been made as to salaries or compensation, a similar deduction will be allowed for services actually rendered.²³

In the case of a foreign partnership the deduction shall be limited to those portions of salaries or compensation which are paid for services rendered with respect to trade or business carried on in the United States.

²² The deductions, allowances and exemptions to be taken in computing net income for the prewar period as well as for the taxable year, are determined by the 1916 Income Tax Law.

²³ For the year 1917 a partnership may deduct a reasonable amount for each partner, calling it salary, whether or not such amount has been paid or agreed to be paid, but in the future such deductions will be allowed only where salary payments to partners are made in accordance with agreements recorded on the books of the partnership. To obtain the benefit of such deductions agreements should at once be made for future payments of salaries to partners.

A partner in his individual capacity is, however, subject to the excess profits tax, if any, at the 8 per cent rate under Art. 15 with respect to any salary or compensation from the partnership for personal services (including any amounts allowed to the partnership as a deduction on his account for the period prior to March 1, 1918).²⁴

Art. 33. Deductions allowed for interest on bona fide loans by partners.—In computing net income for purposes of the excess profits tax a *partnership* will be allowed to deduct amounts paid during the year to an individual partner as interest upon any bona fide loan, but no deduction for so-called interest upon capital will be allowed.

Art. 34. If deduction is made under Art. 32 or 33, corresponding deduction must also be made for prewar period.—If, in computing net income for purposes of the excess profits tax, a *partnership* makes a deduction as allowed by Art. 32 for salaries paid to partners during the taxable year, it must also in computing net income for the prewar period make a corresponding deduction; and if it makes such a deduction as allowed by Art. 33 for interest paid to partners, it must also in computing net income for the prewar period make a corresponding deduction for any such interest actually paid during that period.

NET INCOME—INDIVIDUALS

Art. 35. Determination of net income where there is no invested capital or only nominal capital.—The net income which is derived from a trade or business having

²⁴ The partner is not subject to excess profits tax on his share of the net profits of the partnership, on which the partnership has paid the tax. See Art. 41.

no invested capital or not more than a nominal capital, including salaries, wages, fees or other compensations (constituting net income of class A as defined in Art. 14) shall be determined for the taxable year by adding the total net income from all such sources (or in the case of a *non-resident alien individual* the total net income from all such sources within the United States) as reported for income tax purposes for the same year.

Art. 36. Determination of net income for taxable year when there is invested capital.—The net income which is derived from a trade or business having invested capital (constituting net income of class B, as defined in Art. 14) shall be determined for the taxable year by adding the total net income from such sources (or in the case of a *non-resident alien individual* the total net income from such sources within the United States) as reported for income tax purposes for the same year and deducting therefrom the deduction, if any, for salary allowed by Art. 39, if such deduction has not already been made.

There shall be excluded the amounts received during the year upon the stock or from the net earnings of corporations, joint-stock companies or associations, or insurance companies, subject to the income tax imposed by Title I of the act of September 8, 1916, as amended.

In the case, however, of an individual dealing in securities or otherwise using securities in trade or business there shall be included (1) the amount, if any, received as interest on bonds or obligations of the United States, issued after September 24, 1917 (other than the interest received on an amount of such bonds or obligations the aggregate principal of which does not exceed \$5,000), and (2) such proportion of dividends received upon the stock of foreign corporations as is required to be included by Art. 27.

Illustrations. An individual owns a farm representing an invested capital of \$25,000, a country store with an invested capital of \$6,000, and a flour mill with an invested capital of \$10,000. His net income from the farm is \$4,000, from the store \$3,000, and from the mill \$3,000. Thus his total net income of class B is \$10,000. His total invested capital is \$41,000. Assuming that his deduction is at the rate of 8 per cent his total deduction will be \$3,280 plus \$6,000, or \$9,280, to be applied against his net income of \$10,000 in computing the tax at the graduated rates under Articles 16 and 17.

The same individual allows himself a salary of \$1,000 for working the farm and \$900 for running the store, draws a salary of \$1,200 as president of the local bank, and receives \$250 in compensation for personal services of various kinds, such as road work, helping neighbors in harvest, etc. He also receives \$300 in dividends on an investment in certain stocks, and \$100 as supervisor's fees. The last item—that is, supervisor's fees—is exempt under the law (Sec. 201, subdivision a). The \$300 in dividends is not taxable, inasmuch as it is derived from a mere investment not connected with his trade or business. His net income of class A will therefore consist of his salaries and his compensation for personal services, a total of \$3,350. Since he is entitled to a deduction of \$6,000 as to this class of income, he will have no tax to pay at the 8 per cent rate under Art. 15.

Art. 37. Deduction of contributions for religious, charitable, etc., purposes.—Contributions or gifts for religious, charitable, etc., purposes allowed as a deduction for purposes of the income tax under paragraph "Ninth" of subdivision (a) of Sec. 5 of the act of September 8, 1916, as amended, may, subject to the limitations therein contained, be deducted in computing the net income of

the trade or business for purposes of the excess profits tax only when it is shown to the satisfaction of the Commissioner of Internal Revenue that such contributions or gifts are made by the trade or business and not by the individual in his personal capacity.

Art. 38. Determination of net income for the prewar period where there is invested capital.—The net income which is derived from a trade or business having invested capital (constituting net income of class B as defined in article 14) shall be determined for each of the calendar years 1911, 1912, and 1913 upon the same basis and in the same manner as provided in Art. 36.

Art. 39. Deduction allowed for salary to himself.—An *individual* carrying on a trade or business having an invested capital may in computing the net income of the trade or business for purposes of the excess profits tax deduct a reasonable amount designated by him as salary or compensation for personal service actually rendered by him in the conduct of such trade or business. In no case shall the amount so designated be in excess of the salaries or compensation customarily paid for similar service under like responsibilities by corporations or partnerships engaged in like or similar trades or businesses.

In the case of a *non-resident alien individual*, the amount deducted shall be limited to that portion of the salary or compensation which is for service rendered with respect to trade or business carried on in the United States.

The amount so designated shall, however, be included in computing his net income of class A under Art. 35; and the balance of the income from his trade or business shall be included in computing his net income of class B under Art. 36.

Illustrations. An individual owns and runs a news-

paper having an invested capital of \$50,000. The net income from the newspaper, without making any allowance for the salary of the owner, is \$20,000, and, as income of class B, is subject to the graduated rates prescribed in Art. 16. His deduction, as provided for in subdivision (b) of Art. 21, would be \$4,500 (9 per cent of his capital) plus \$6,000, a total of \$10,500. If, however, he allows himself a salary of \$3,000, the net income from the newspaper will be \$17,000, and the deduction of \$10,500 will be applied against that amount.

His salary of \$3,000 must be included in his return as income of class A, which is subject to the 8 per cent rate under Art. 15. If it constitutes his only income of that class he will pay no tax thereon, inasmuch as it is less than the deduction of \$6,000 to which he is entitled as to that class of income. But if, for example, he receives in addition a salary of \$4,000 as president of the local bank, his total net income of class A will be \$7,000, and he will be required to pay a tax of 8 per cent on \$1,000 thereof, or \$80.

Art. 40. If deduction is made under Art. 39 corresponding deduction must also be made for prewar period.—If, in computing net income for purposes of the excess profits tax, an individual deducts a reasonable amount designated as salary or compensation for personal services rendered by himself, as allowed by Art. 39, he must also in computing net income for the prewar period, make a corresponding deduction.

Art. 41. Individual member of partnership.—Inasmuch as a partner in his individual capacity is not considered to be engaged in trade or business with respect to his share in the profits of the partnership, he is not subject to excess profits tax thereon. Consequently, in computing his net income for purposes of the excess profits

tax he need not include his share of the partnership profits.

He shall, however, in computing his net income of class A under Art. 35, include any salary or compensation from the partnership for personal services (including any amount allowed to the partnership as a deduction on his account for the period prior to March 1, 1918, in accordance with Art. 32.)

INVESTED CAPITAL—GENERAL PROVISIONS

Art. 42. Allowance for depletion, depreciation, and obsolescence in computation of invested capital.—The term "invested capital" as used in the excess profits tax law means the invested capital of the present owner. The basis, or starting point, in the computation of invested capital is found in the amount of cash and other property paid in, the original values of such other property being determined in accordance with the rules laid down in these regulations. But the computation does not stop with such original entries or amounts; it must take properly into account the surplus and undivided profits. In the computation of surplus and undivided profits, however, full recognition must first be given to expenses incurred and losses sustained from the original organization of the business concern down to the taxable year, including among such expenses and losses a reasonable allowance for depletion, depreciation, or obsolescence of property originally acquired for cash or for stock or shares or in any other manner.²⁵ If value appreciation

²⁵ The question of depreciation and other losses presents many difficulties. It is clear that depreciation, depletion and losses must be deducted to reduce the surplus and undivided profits accounts to their present value, since the law allows only surplus and undivided profits *used and employed in the business*

of a kind not subject to income tax (other than that allowed under Art. 55) has been taken up in the accounts, a deduction must be made in respect of such appreciation so taken up. In the computation of the invested capital for any year full effect must also be given to any liquidation of the original capital.

Art. 43.—How to ascertain average invested capital for the year, averaged monthly.—The invested capital for any prewar or taxable year (or where the tax is computed upon the basis of a period less than a year, for such period) is the average invested capital for the year or period averaged monthly, according to the following rules:

(a) Add the capital for each of the several months during which no change occurs, and the average capital (ascertained as provided in subdivision (b) of this article) for each month in which a change occurs and divide the total by the number of months in the year or period.²⁶

(b) To ascertain the capital for any month in which a change occurs multiply the capital as of the first day of

to be included as invested capital. But the law contains no requirement that cash or property paid in by the stockholders or members shall be used or employed in the business. The intent seems to be to require a deduction based on the capital originally paid in whether or not such amount has been reduced by losses. A corporation, for instance, to which a certain amount of capital was once contributed, and which has not paid back any part thereof to its stockholders, either directly or indirectly, should be allowed to claim deduction on the entire amount originally paid in regardless of losses which may have impaired such capital.

²⁶ To illustrate: If the corporation has been engaged in business for six months with an invested capital of \$100,000 for each of such months, the invested capital will be ascertained by dividing \$600,000 by 6—not by 12. But the deduction ascertained on that basis will be divided by 2. See Art. 20.

the month by the number of days it remains constant and the capital after each change by the number of days (including the day on which the change occurs) during which it remains constant, add the products, and divide the sum by the number of days in the month.

Art. 44. Items not allowed to be included in invested capital.—The second paragraph of Sec. 207 of the excess profits law specifies certain items which may not be included in invested capital, namely:

(a) Stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to the excess profits tax; and

(b) Money or other property borrowed.

The term "money or other property borrowed" as used in Sec. 207 and these regulations includes not only cash or other borrowed property which can be identified as such, but current liabilities and temporary indebtedness of all kinds, and any permanent indebtedness upon which the taxpayer is entitled to an interest deduction in computing net income. A corporation which under the income-tax law is allowed to deduct only a part of the entire interest paid upon its indebtedness, may include in its invested capital such a proportion of its permanent indebtedness as the amount of interest upon such indebtedness which the corporation is not allowed to deduct is of the total amount of interest paid upon such indebtedness during the taxable year.

Art. 45. When income from tax-free securities consists partly of trading profits and partly of interest, dividends, etc.—Whenever income consists partly of gains or profits subject to the excess profits tax arising from trading in stocks, bonds, etc., the dividends or interest on which are not subject to such tax, and partly of such dividends or interest, then, subject to the limita-

tions as to borrowed money, there shall be included in the invested capital an amount which bears the same ratio to the total amount invested in such stocks or bonds as the amount of such gains or profits bears to the total amount of such income.

Art. 46. Treatment of stock of foreign corporations when held by domestic corporations or partnerships or by citizens or residents of the United States.—In the case of *domestic corporations or partnerships* and of *citizens or residents* of the United States holding stock in a foreign corporation part of whose net income is subject to the income tax, there shall be included in invested capital such proportion of the value of the stock in such foreign corporation as the net income of such foreign corporation from sources outside the United States is of its entire net income.²⁷

Art. 47. Construction of terms "tangible property" and "intangible property."—The term "other intangible property" as used in Sec. 207 will be construed to mean property of a character similar to good will, trademarks, and the other specific kinds of property enumerated in the same clause. With respect to property not clearly of such a character, rulings will be issued as occasion may demand to indicate whether it shall be regarded as tangible or intangible.

The following classes of property when paid in for stock or shares in a corporation or partnership, will be regarded as tangible property so paid in:

- (a) Stocks.
- (b) Bonds.

²⁷ That is, to the extent that the dividends are included in income the stock may be included in invested capital. See Art. 27.

- (c) Bills and accounts receivable.
- (d) Notes and other evidences of indebtedness.
- (e) Leaseholds.

But when a corporation pays for intangible property by the issuance of its own stock or bonds, this will not be regarded as being a payment bona fide made in cash or tangible property within the meaning of Sec. 207.

Art. 48. Invested capital of foreign corporations or partnerships or non-resident alien individuals.—When used with reference to a *foreign corporation or partnership* or a *non-resident alien individual*, the term “invested capital” means that proportion of the entire invested capital as defined and limited by these regulations which the net income from sources within the United States is of the entire net income.

Art. 49. Reorganization on or after January 2, 1913.—A trade or business carried on by a *corporation, partnership, or individual*, which has been formally organized or reorganized on or after January 2, 1913, but which is substantially a continuation of a trade or business carried on prior to that date, shall, for the purposes of the excess profits tax, be deemed to have been in existence prior to that date and the invested capital of its predecessor prior to that date shall be deemed to have been its invested capital. This article relates to the prewar period and does not apply to the invested capital for the taxable year.²⁸

Art. 50. Reorganization after March 3, 1917.—In case of the reorganization, consolidation, or change of ownership of a trade or business after March 3, 1917, if an interest or control in such trade or business of 50 per cent or more remains in control of the same persons, cor-

²⁸ See Art. 22.

porations, associations, partnerships, or any of them, then in ascertaining the invested capital of the trade or business no asset transferred or received from the prior trade or business shall be allowed a greater value than would have been allowed under these regulations in computing the invested capital of such prior trade or business if such asset had not been so transferred or received, unless such asset was paid for specifically as such, in cash or tangible property, and then not to exceed the actual cash or actual cash value of the tangible property paid therefor at the time of such payment.

Art. 51. Invested capital for prewar period.—The invested capital for the prewar period shall, in general, be determined in the same manner as for the taxable year, except that the valuation as of January 1, 1914, shall not apply to tangible property paid in for stock or shares.²⁹

Art. 52. Scope of Sec. 210.—Sec. 210 provides for exceptional cases in which the invested capital can not be satisfactorily determined. In such cases the taxpayer may submit to the Commissioner of Internal Revenue evidence in support of a claim for assessment under the provisions of Sec. 210.³⁰ Such exceptional cases may consist, among others, of the following:

(1) Where, through defective accounting or the lack of adequate data, it is impossible accurately to compute invested capital.

(2) Where upon application by a foreign taxpayer the Secretary of the Treasury finds that the expense of securing the data necessary for the computation of the invested capital would be unreasonable in view of the amount of tax involved, or that it is impracticable to

²⁹ See Art. 55.

³⁰ See Arts. 18 and 24.

determine either the "entire invested capital" or the "entire net income."

(3) Long-established business concerns which by reason of ultra-conservative accounting or the form and manner of their organization would, through the operation of Sec. 207, be placed at a serious disadvantage in competing with representative concerns in a like or similar trade or business.

(4) Where the invested capital is seriously disproportionate to the taxable income. Such cases may arise through:

(a) The realization in one year of the earnings of capital unproductively invested through a period of years or of the fruits of activities antedating the taxable year; or,

(b) Inability, to recognize or properly allow for amortization, obsolescence, or exceptional depreciation due to the present war, or to the necessity in connection with the present war of providing plant which will not be wanted for the purposes of the trade or business after the termination of the war.

INVESTED CAPITAL—CORPORATIONS AND PARTNERSHIPS

Art 53. Rule for computing invested capital.—In computing invested capital, every corporation or partnership paying taxes at the graduated rates prescribed in Sec. 201,³¹ shall add together its *paid-in capital* and its *paid-in or earned surplus and undivided profits* (under whatever name the same may be called) as shown by its books at the beginning of the taxable year. The total thus obtained shall be adjusted for any asset or item which it covers that is not carried on the books at the

³¹ See Art. 16.

valuation prescribed by law or by these regulations. When necessary, adjustment (addition or subtraction) shall be made in respect of the following:

ADJUSTMENTS

1. Stock or shares issued in the purchase of intangible property prior to March 3, 1917, which cannot be included in an amount exceeding (a) 20 per cent of the par value of the total stock or shares outstanding on that date, (b) the actual value of such intangible property at the date acquired, or (c) the par value of the stock or shares issued in payment therefor, whichever is the lowest.³²

2. Stock or shares issued for a mixed aggregate of tangible property, patents and copyrights, and good will or other intangible property.³³

3. Stock or shares issued for patents and copyrights, valued at (a) their actual cash value at the time of payment, or (b) the par value of the stock or shares issued therefor, whichever is lower.³⁴

4. Stock or shares issued for tangible property prior to January 1, 1914, valued at (a) the actual cash value of such property on January 1, 1914, or (b) the par value of the stock, whichever is lower.³⁵

5. Stock originally issued for property and subsequently returned to the corporation as a gift, etc.³⁶

6. Add any proportion of its permanent indebtedness which may be included under Art. 44.

7. Add value of tangible property paid in for stock or

³² See Arts. 57 and 58.

³³ See Art. 59.

³⁴ See Art. 56.

³⁵ See Art. 55.

³⁶ See Art. 54.

shares in excess of the par value of such shares, when authorized by Art. 63.

8. Add amounts expended in the past for (a) the acquisition of tangible property or (b) specifically for good will and other similar intangible property, when authorized by Art. 64.

9. For the valuation of assets acquired in reorganizations, etc., (a) effected after March 3, 1917, see Art. 50; (b) as to the prewar period, see Articles 49 and 51.

10. Deduct amounts representing appreciation excluded by Art. 42.

11. Make any additional deductions required by reason of insufficient allowances in the accounts of the taxpayer for depletion, depreciation, and obsolescence.³⁷

Whenever any corrections are made in respect of the capital stock and surplus, corresponding corrections must be made in the respective asset items in the balance sheet of the taxpayer.

After making any adjustments required under Paragraphs 1 to 11 above, the adjusted total of the capital and surplus account will represent the invested capital at the beginning of the taxable year, except that in any case where the admissible assets (and these include all assets when valued in accordance with these regulations, except stocks, bonds—other than obligations of the United States—the income of which is not subject to excess-profit tax) are less than the amount of such adjusted total, then the invested capital must be further reduced to an amount equal to the sum of the admissible assets. Tax-free securities and stock in foreign corporations may be included as admissible assets *to the extent* authorized in Articles 45 and 46.

³⁷ See Art. 42.

If there has been any change made during the taxable year in the amount of the invested capital, the monthly average shall be taken,³⁸ but in no case may the invested capital include any surplus or undivided profits earned during the taxable year.³⁹

With respect to the taxable year 1917, every such corporation and partnership will be required to submit a balance sheet as at the first day of the taxable year and also a balance sheet as at the close of the taxable year. Thereafter every such corporation and partnership will be required to submit a balance sheet as at the close of each taxable year. Balance sheets should be made in accordance with the books of the taxpayer and changes in respect of any items therein made pursuant to these regulations should be explained in a separate statement attached to the balance sheet to which it relates.

Art. 54. Stock returned to corporation.—For the purpose of computing invested capital, in cases where the stock of a corporation is issued or exchanged for property (tangible or intangible), the following rule will apply:

When any of such stock is returned to the corporation as a gift or for a consideration substantially less than its par value, the stock so returned shall not be treated as a part of the stock issued or exchanged for such property. The proceeds derived in cash or its equivalent from the resale of the stock so returned shall, however, be included in the invested capital if retained and employed in the business.

Art 55. Valuation of tangible property paid in for stock or shares.—Tangible property paid in for stock or shares prior to January 1, 1914, must be valued at

³⁸ See Art. 43.

³⁹ See Art. 61.

either (a) the actual cash value of such property on January 1, 1914, or (b) the par value of the stock or shares specifically issued therefor, whichever is lower. This is one of the few cases in which the law permits allowance to be made for appreciation, and here no appreciation can be recognized unless the original stock or shares were *specifically* issued in exchange for such tangible property.

Tangible property paid in for stock or shares on or after January 1, 1914, will be taken at the actual cash value of such property at the time of payment, irrespective of the par value of the stock or shares.

Art. 56. Patents and copyrights.—Patents and copyrights paid in for stock or shares must be valued at either (a) the actual cash value at the time of payment or (b) the par value of the stock or shares issued therefor, whichever is lower.

Art. 57. Valuation of intangible property.—If good will, trademarks, trade brands, franchises of a corporation or partnership, or other intangible property has been purchased with stock or shares issued prior to March 3, 1917, the amount that may be included in invested capital must not exceed (a) 20 per cent of the par value of the total stock or shares outstanding on that date, nor (b) the actual value of the asset at the date acquired, nor (c) the par value of the stock issued in payment for the asset.

Art. 58. Application of 20 per cent limitation upon intangible property.—The 20 per cent limitation upon intangible property purchased prior to March 3, 1917, for or with stock or shares of the corporation or partnership, applies not to each item or class of intangible property separately, but to the aggregate amount of all such property so purchased. Such intangible property may be included in the invested capital only up to an amount

not exceeding 20 per cent of the total stock or shares of the corporation or partnership on March 3, 1917, even though the aggregate amount of such intangible property be greater in value than such 20 per cent of the par value of the total stock or shares.

Intangible property bona fide purchased prior to March 3, 1917, with stock having no par value may be included in invested capital at a value not exceeding the actual cash value of such intangible property at the time of the purchase and in an amount not exceeding 20 per cent of the total shares of stock outstanding on March 3, 1917, measured by their value as at the date or dates of issue.

Art. 59. Rules to govern cases where shares or securities are issued for mixed aggregate of tangible and intangible property.—Where stock or shares (or stock or shares and bonds or other obligations) have, prior to March 3, 1917, been issued for a mixed aggregate of—

- (a) Tangible property,
- (b) Patents and copyrights, and
- (c) Good will or other intangible property,

the following rules will govern :

(1) In the absence of satisfactory evidence to the contrary, it will be presumed in the case of a corporation, that its stock was issued for the following purposes in the order named :

- (a) Good will or other intangible property,
- (b) Patents and copyrights, and
- (c) Tangible property.

(2) Upon the production by the taxpayer of evidence satisfactory to the Commissioner of Internal Revenue as to the actual values at the date of acquisition of (a) the tangible property and (b) the patents and copyrights, the sum of these two items may be applied against the

total par value of the securities issued and the remainder will then be deemed to represent the par value of the securities issued for the good will or other intangible property.

(3) Cases where mixed aggregates of tangible and intangible property have been paid in for stock and bonds shall, if the Secretary of the Treasury is unable to determine satisfactorily the respective values of the several classes of property at the time of payment be treated as coming under Articles 18 and 24 and the tax shall be, assessed accordingly.

Art. 60. Valuation of intangible assets purchased.

—Good will and other similar intangible assets purchased with cash or tangible property must be taken at a value not in excess of the cash or actual cash value of the tangible property specifically paid therefor.

Art. 61. Surplus or undivided profits earned during any year excluded in computing invested capital for such year.—Profits earned during any taxable year or prewar year shall not be included in the computation of the invested capital for such year, even though set up as “surplus” upon the books or distributed in the form of stock dividends.⁴⁰

⁴⁰ Sec. 207, Subdiv. (a) provides that there may be included as invested capital “paid in or earned *surplus and undivided profits* used or employed in the business, exclusive of *undivided profits* earned during the taxable year.” A liberal construction of this language would permit the inclusion of such amounts of the earnings of the taxable year as are in fact actually and permanently employed as additional capital in the business. The omission of the word surplus in the second clause of the language quoted is not without significance; the use of the phrase “undivided profits,” when the word “profits” would clearly have excluded all earnings of the year, also supports a liberal construction. It is manifestly just to allow credit for addi-

Art. 62. Scope of phrase "surplus and undivided profits."—Clause (3) of subdivision (a) of Sec. 207 authorizes the inclusion in invested capital of earned surplus and undivided profits used or employed in the business. Inasmuch as Sec. 201 provides that all the income of a corporation or partnership shall be deemed to be received from its trade or business, all the surplus and undivided profits of a corporation or partnership (exclusive of undivided profits earned during the year), from whatever source derived, will, unless invested in stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to the excess profits tax, be deemed to be used or employed in the business and may be included in the invested capital.

Art. 63. When tangible property may be included in surplus.—Where it can be shown by evidence satisfactory to the Commissioner of Internal Revenue that tangible property has been conveyed to a corporation or partnership by gift or at a value, accurately ascertainable or definitely known as at the date of conveyance, clearly and substantially in excess of the cash or the par value of the stock or shares paid therefor, then the amount of the excess shall be deemed to be paid in sur-

tional capital employed during the year when the earnings therefrom are added to the taxable income. The difficulty of distinguishing between current earnings actually re-invested in the business during the year and earnings merely accumulated for distribution at the end of the year may have militated against a broader construction of this provision. But in any event the declaration of a stock dividend would be a clear indication, for by such act the profits become capital and are taken out of the class of surplus and undivided profits. Art. 69 permits the inclusion of profits earned during the taxable year in computing the invested capital of individuals.

plus. The adopted value shall not cover mineral deposits or other properties discovered or developed after the date of conveyance, but shall be confined to the value accurately ascertainable or definitely known at that time.⁴¹

Evidence tending to support a claim for a paid-in surplus under these circumstances must be as of the date of conveyance, and may consist, among other things, of (1) an appraisal of the property by disinterested authorities, (2) the assessed value in the case of real estate, and (3) the market price in excess of the par value of the stock or shares.⁴²

Art. 64. Reconstruction of surplus and undivided profits accounts.—Where through failure to provide for depletion, depreciation, obsolescence, or other expenses or losses, or where for any other cause or reason the books of account of the taxpayer do not show the true paid-in or earned surplus and undivided profits, in the computation of invested capital such adjustments shall be made as are necessary to arrive at a statement of the correct amount.

Where a taxpayer claims additions to the capital account, the books of account will be presumed to show the true facts and the burden of proof will rest upon the taxpayer. Such additions will be accepted only to the extent and under the conditions stated below:

(1) Amounts which have been expended in the past for the acquisition of plant, equipment, tools, patterns,

⁴¹ This ruling is supported by the language of the statute (Sec. 207a) which permits the inclusion of "the actual cash value of tangible property paid in * * * at the time of such payment."

⁴² The three methods outlined are not exclusive. Other evidence may be submitted to show the value at the time of acquisition.

furniture, fixtures, or like tangible property, having a useful life extending substantially beyond the year in which the expenditure was made, and which have been charged as current expense, may (less proper reduction for depreciation or obsolescence) be added to the surplus account in computing invested capital when such assets are still owned and in active use by the taxpayer during the taxable year. Special tools, patterns, and similar assets shall not be assigned any value if their cost has been recovered through having been included in the price of goods. If their cost has not been so recovered and they are held for only occasional use, they shall not be assigned a value in excess of the fair value based upon the earnings actually arising from their current use. Assets of this kind not in current use shall not be valued at more than their nominal or scrap value.

(2) Amounts expended in the past for good will, trademarks, trade-brands, franchises, and other intangible assets of a like character, are controlled by the language of the statute which provides that such assets "shall be included in invested capital if the corporation or partnership made payment bona fide therefor specifically as such in cash, or tangible property." The Commissioner of Internal Revenue will recognize additions to invested capital on account of intangible assets only if such assets have been explicitly paid for in the manner prescribed by the statute. Where expenditures have been made for the general development of intangible assets, and charged as current expense, no readjustment thereof will be allowed.⁴³

⁴³ Amounts expended prior to March 1, 1913, in, for instance, litigation to protect patents are proper additions to the cost of the patents, but whether or not advertising expense is a proper addition to the investment in good will, trade marks, etc., depends upon the circumstances in each particular case.

(3) Amounts under (1) and (2) above, expended on or after March 1, 1913, will, in the case of a corporation, be limited strictly to items which have not been deducted in computing taxable income upon its income tax return. Whenever a corporation has claimed and the department has allowed a deduction in respect to its income tax, the item upon which the deduction is based shall not be restored to the surplus account nor included in the invested capital.

(4) The taxpayer shall in his return to the Commissioner of Internal Revenue make a statement of the proposed additions, specifying the kinds and amounts of property involved, the years in which the expenditures were made, and the method followed in distinguishing between capital outlays and current expenses.

(5) The taxpayer shall also show that adequate provision has been made for the depletion, depreciation, or obsolescence of such of the assets so acquired as are, under the rulings of the department, subject to recognized depreciation.

Art. 65. Invested capital of insurance companies.—

(a) The invested capital of a *mutual insurance company* will be deemed to consist of the sum of (1) any surplus or contingent reserves maintained for the general use of the business, plus (2) any legal reserves the net additions to which are included in the net income subject to the tax—subject to the restrictive provisions of Art. 44 requiring the exclusion of tax-free assets other than obligations of the United States.

(b) The invested capital of a *stock insurance company* will be deemed to consist of its capital stock, paid in or earned surplus and undivided profits (subject to the same restrictive provision of Art. 44), computed in accordance with the provisions of Art. 53.

INVESTED CAPITAL—INDIVIDUALS

Art. 66. Items included in invested capital.—Subject to the limitations stated in these regulations,⁴⁴ the invested capital of an individual is measured by the total of three items:

- (1) Actual cash paid into the trade or business.
- (2) Tangible property paid into the trade or business.
- (3) Patents and copyrights, and good will, trade-marks, trade-brands, franchises, and other intangible property.^{44a}

Art. 67. Valuation of tangible property.—Subject to the requirements of Art. 42 as to allowance for depletion, depreciation and obsolescence, valuation of tangible property will be as follows:

In the case of tangible property purchased with cash the valuation will be based upon the cost (estimated if not known) in cash at the time purchased.

In the case of tangible property paid in as such prior to January 1, 1914, the valuation will be based upon its actual cash value as of that date. Adequate evidence of such value must be furnished by the taxpayer.⁴⁵

In the case of tangible property paid in on or after January 1, 1914, the valuation will be based upon its actual cash value at the time of payment.

It will be presumed that the tangible assets employed in the trade or business have been acquired with cash which has been either paid in directly or derived from earnings of the trade or business; but the taxpayer will

⁴⁴ See Arts. 42 to 52 inclusive.

^{44a} See Art. 68.

⁴⁵ See Art. 63.

be entitled to show that such assets were paid in as tangible property.

Art. 68. Valuation of intangible property.—Patents and copyrights, and good will, trade-marks, trade-brands, franchise, and other similar intangible assets may be included in invested capital at a value not to exceed the actual cash paid therefor or the actual cash value at the time of payment of the tangible property paid therefor, but only if bona fide payment was made therefor specifically as such in cash or tangible property.⁴⁶

Art. 69. Profits earned during taxable year may be included.—The restriction in respect of undivided profits earned during the taxable year which is imposed upon corporations and partnerships does not apply to individuals, and therefore, unless otherwise shown, the profits of the taxable year remaining in the trade or business will be deemed to have arisen ratably throughout the year, and the capital at the beginning of the year may be increased by the total amount of such profits remaining in the trade or business averaged monthly over the year.⁴⁷

Art. 70. Rule for computing invested capital.—Where an individual keeps books of account his invested

⁴⁶ Amounts spent in litigation to protect patents, copyrights or trade marks and amounts spent in advertising to establish trade names, etc., it seems, can be held to be additional investments of capital if not charged to expense and proof can be produced to show the disbursements to have been made specifically for such purposes. "Other similar intangible assets" would include licenses, rights to manufacture under letters patent, etc.

⁴⁷ The individual may, if he keeps books, show that the greater part of the year's earnings accrued in the earlier months of the year, in which case the deduction will be greater than if the earnings are considered to have arisen ratably. See Art. 43 for manner of determining monthly average.

capital will be found in his capital account (under whatever name it may be called) after making therein any adjustments or corrections required by these regulations,⁴⁸ provided that the assets other than those not allowed to be included equal or exceed the amount of such capital account.⁴⁹ Otherwise the invested capital shall be the amount of such assets.

Where an individual does not keep books of account he should prepare and preserve a statement as at the beginning of the taxable year and as at the end of the taxable year, showing in full all his assets valued in accordance with these regulations, and all his liabilities. The excess of such assets over such liabilities at the beginning of the year and again at the end of the year will constitute the invested capital of the individual on those dates, respectively, provided, that in each case the assets other than those not allowed to be included equal or exceed the amount of such excess. Otherwise the invested capital shall be the amount of such assets. The amount of the difference between the capital thus shown as at the beginning of the year and at the end of the year will, in the absence of evidence to the contrary, be deemed to have arisen ratably throughout the year, and the capital at the beginning of the year will be increased or decreased, as the case may be, by such amount averaged monthly over the year.

⁴⁸ The adjustments and corrections referred to are evidently the ones described in Arts. 42 to 52 inc. See also Art. 53, paragraphs 8, 10 and 11.

⁴⁹ That is, if the assets other than those described in Art. 44 equal the capital account, all of such account may be considered as invested capital. In other words, the assets which are excluded by Art. 44 are used first to offset borrowed money, and only the amount in excess of borrowed money is applied to reduce the capital account.

If an individual is engaged in more than one trade or business having invested capital, then his invested capital for the purposes of computing the deduction and applying the rates of taxation will be determined by taking the total invested capital of all such trades or businesses.

The terms "assets" and "liabilities" as used in this article relate only to the assets or liabilities of the trade or business.

NOMINAL CAPITAL

Art. 71. Application of Section 209.—Sec. 209 (see Art. 15) applies primarily to occupations, professions, trades, and businesses engaged principally in rendering personal service in which the employment of capital is not necessary and the earnings of which are to be ascribed primarily to the activities of the owners.

In determining whether a trade or business is taxable under Art. 15 no weight will be given to the fact that it is carried on by means of personal service unless the principal owners are regularly engaged in the active conduct of the trade or business.

Art. 72. Application of Section 209 not to be affected by mere size of capital, form of organization, etc.—Business concerns which render professional or personal service and are of the class normally taxable under Art. 15 shall not be taken out of that class merely because of the size of the capital if the employment of such capital is necessitated by delay and irregularity in the receipt of fees, etc., or if such capital is wholly or mainly used as a fund from which to advance salaries, wages, etc., or to provide office furniture, accommodations, and equipment, nor because of the form of organization, whether corporation or partnership, nor in the case of a partnership because of the number of partners.

Art. 73. Agents and brokers.—Agents and brokers requiring and using no capital or merely a nominal capital in their business are taxable under Art. 15, but commission houses regularly employing a substantial amount of capital, whether to lend to principals or to carry goods on their own account, are not deemed to be agents or brokers and are taxable under the provisions of Art. 16.

Art. 74. Meaning of "nominal capital;" businesses which will not be deemed to have nominal capital.—The term "nominal capital" as used in Sec. 209 means in general a small or negligible capital whose use in a particular trade or business is incidental. The following will not be construed as businesses having a nominal capital for purposes of excess profits tax:

(a) A business which because of conditions arising from the war or exceptional opportunities for profits earns a disproportionately high rate of profit during the taxable year, if it belongs to a class which necessarily and customarily requires capital for its operation. In the determination of doubtful cases stress will be laid upon the normal relation of net income to capital during pre-war years;

(b) Corporations which, although their capitalization is nominal, employ a substantial amount of capital in their business;

(c) A business having a substantial capital, but whose invested capital within the meaning of Sec. 207 is reduced to a nominal amount by the operation of the restrictive clauses of that section, e. g., where the capital, consisting originally of a small amount of cash paid in, has since appreciated in value, or where the capital is largely covered by indebtedness or consists principally of tax-free securities or of intangible assets built up or

developed by expenditures which have been regularly deducted as items of current expense.⁵⁰

RETURNS

Art. 75. When a return of information as to the invested capital and net income for the prewar period will not be required.—For the purposes of the excess profits tax, a return of information with respect to the invested capital and net income *for the prewar period* will not be required of a corporation, partnership, or individual in the following cases:

(1) If the taxpayer accepts the minimum percentage, viz., 7 per cent, as the percentage to be used in computing the deduction under Art. 21; or

(2) If the trade or business is taxable only at the 8 per cent rate under Art. 15.

This article must not be construed as not requiring a return of information as to all facts which may be necessary for the ascertainment of the capital and income *for the taxable year* whenever such a return is required by the Commissioner of Internal Revenue.

Art. 76. A married woman may make separate return.—A married woman who is a sole trader or is entitled to any taxable income to her sole and separate use may,

⁵⁰ It will be noted that these rulings do not so much attempt to define "nominal capital" as to define or outline the kinds of businesses which are or can be carried on without the use of capital, except incidentally, and in which the profits depend primarily on the services of the individuals in the business. If the use of capital is essential, and the services of the individuals are incidental, the business does not come within the purview of Sec. 209, merely because the amount of "invested capital" is small as compared with the profits. Where borrowed money enters largely into the capital of the business, see Art. 44.

for purposes of the excess-profits tax, make a separate return in the same manner as any other individual.

Art. 77. When affiliated corporations must furnish information as to intercorporate relations.⁵¹—For the purpose of the excess profits tax every corporation will describe in its return all its intercorporate relationships with other corporations with which it is affiliated, and will furnish such information in relation thereto as will enable the Commissioner of Internal Revenue to compute the amount of the tax properly due from each corporation on the basis of an equitable and lawful accounting.

For the purpose of this regulation two or more corporations will be deemed to be affiliated (1) when one such corporation owns directly or controls through closely affiliated interests or by a nominee or nominees, all or substantially all of the stock of the other or others, or when substantially all of the stock of two or more corporations is owned by the same individual or partnership, and both or all of such corporations are engaged in the same or a closely related business; or (2) when one such corporation (a) buys from or sells to another products or services at prices above or below the current market, thus effecting an artificial distribution of profits, or (b) in any way so arranges its financial relationships with another corporation as to assign to it a disproportionate share of net income or invested capital.

⁵¹ This and the following paragraph recognize the unity of a business carried on by means of two or more separate corporations between which strict accounting of profits may not have been observed. By considering the affiliated corporations as a unit and consolidating the invested capital and the income of all, an average ratio of earnings to invested capital is reached for the business as a whole.

Art. 78. When affiliated corporations may be required to make consolidated return.—Whenever necessary to more equitably determine the invested capital or taxable income, the Commissioner of Internal Revenue may require corporations classed as affiliated under Art. 77 to furnish a consolidated return of net income and invested capital. Where such consolidated return is required it may be made by any one or more of such corporations or by all of them acting jointly; but if such affiliated corporations, when requested to file such consolidated return, neglect or refuse to do so, the Commissioner of Internal Revenue may cause an examination of the books of all such corporations to be made and a consolidated statement to be made from such examination. In cases where consolidated returns are accepted, the total tax will be computed in the first instance as a unit upon the basis of the consolidated return and will be assessed upon the respective affiliated corporations in such proportions as may be agreed among them. If no such agreement is made the tax will be assessed upon each such corporation in accordance with the net income and invested capital properly assignable to it.

ASSESSMENT AND COLLECTION

Art. 79. Assessment and collection governed by income tax regulations.—All excess profits taxes to which any taxpayer is subject shall be assessed and collected at the same times and in the same manner as provided with respect to income taxes in the income tax regulations in so far as the same are applicable.

CHAPTER 47

THE STAMP TAX

The present stamp tax is imposed under the provisions of Title VIII. of the War Revenue Act of October 3, 1917. It is to some extent a re-enactment of the Act of October 22, 1914, but contains several changes, and some of the instruments which were taxed under the former law are omitted, such as bills of lading, express receipts, certificates of profit, certificates of damage, certificates of any description not otherwise specified, brokers' notes or memoranda of sale, insurance policies, and protests. The present law does not contain Schedule B of the Act of October 22, 1914, which provided for a tax on perfumery, cosmetics and similar articles, and chewing gum or substitutes therefor. The present law went into effect on December 1, 1917, except as to the tax on playing cards, which became effective on October 4, 1917. The phrase "incidence of tax" is used in this chapter to mean the time when the tax was first applied under the statute. A list of the several instruments taxable under the present law, together with the rates of tax applicable to each and the rulings which have been made with respect to each are given in the following paragraphs.¹

Bonds of Indebtedness. Bonds, debentures or certificates of indebtedness issued on and after December 1, 1917, by any person, corporation, partnership, or association, are taxable at the rate of five cents on each one

¹ In this list is also included reference to a number of instruments which are not taxable under the present law. These references are inserted for the convenience of the reader who may be searching for positive assurance that a particular instrument need not be stamped.

hundred dollars of face value or fraction thereof. Under the former law² the tax was imposed only on bonds issued by corporations or associations. It is to be noted that the present act imposes the tax on bonds issued by persons and partnerships as well. There is no clear distinction between bonds of indebtedness and promissory notes and it is sometimes difficult to determine whether an instrument should be taxed under the higher rate applying to bonds of indebtedness or the lower rate applying to promissory notes. The name on the instrument is not always conclusive. Thus, under the former law it was held that an instrument designated as a "gold note" issued in the amount of \$1,000 with interest coupons attached, and containing a promise by a corporation to pay a certain sum of money to the holder thereof under certain terms and conditions prescribed by the indenture of trust was more in the nature of a bond or certificate of indebtedness than a promissory note and was, therefore, held taxable as a bond.³

BONDS GIVEN IN A PENAL SUM. When a bond conditioned for the repayment or payment of money is given in a penal sum greater than the debt secured, the tax is based upon the amount secured and not upon the amount of the bond.⁴

RENEWAL OF BONDS. Every renewal of a bond, debenture of certificate of indebtedness is taxed as a new issue.⁵

TRANSFER OF BONDS. No tax is imposed upon the transfer of bonds, debentures or certificates of indebtedness from one holder to another.

² The expression "former law" is used herein to indicate the Act of October 22, 1914.

³ T. D. 2257. See definition under Promissory Notes, *infra*.

⁴ Act of October 3, 1917, Section 807, Schedule A-1.

⁵ *Id.*

CERTIFICATES OF DEPOSIT. Certificates of deposit issued by banks and trust companies are not taxable under this head.⁶ Such certificates were held not to be taxable under the former law.

ISSUE OF BONDS. It seems generally that the delivery of the bond establishes the date of issue. Thus, it was held under the former law that bonds certified and delivered by a trustee after the incidence of the tax were taxable although subscribed and paid for prior thereto. Under the stamp tax law of 1898 it seems to have been held that a bond was issued when delivery was made and the corporation received a benefit or a consideration therefor.⁷ The date of renewal would be the date of issue for the purpose of the tax on renewal of bonds.⁸ Bonds issued by a domestic corporation in this country for sale to purchasers in a foreign country were held to be issued here for the purpose of the tax, but bonds issued and sold by a domestic corporation in a foreign country were not required to be stamped on the ground that the Government had no means of enforcing the statute in such case.⁹

WHERE STAMPS AFFIXED. Under the former law it was held that the stamps denoting the tax should be affixed to the bonds, unless temporary bonds were issued, in which case the stamps could be affixed to the indenture, the temporary bonds and definitive bonds having printed or engraved thereon a notation that the stamps were affixed to the indenture.¹⁰

⁶ T. D. 2054; letter from Treasury Department dated Nov. 16, 1917.

⁷ Volume 1, Treasury Decisions No. 20156.

⁸ Every renewal is taxed as a new issue. Act of October 3, 1917, Sec. 807, Schedule A-1.

⁹ Letter from Treasury Department dated May 15, 1915.

¹⁰ T. D. 2164, T. D. 2220.

Bonds of Indemnity and Surety. Bonds coming within this class are (a) bonds for indemnifying any person, corporation, or partnership, who shall have become bound or engaged as surety, (b) all bonds for the due execution or performance of any contract, obligation, or requirement, or the duties of any office or position, and to account for money received by virtue thereof, and (c) all other bonds of any description not otherwise provided for in the law. There are two express exemptions from the tax imposed by this subdivision: (a) such bonds as may be required in legal proceedings and (b) policies of reinsurance. The rate of tax is fifty cents unless a premium is charged for the execution of such bonds, in which case the tax is one per cent of each dollar or fractional part thereof of the premium charged.

BONDS REQUIRED IN LEGAL PROCEEDINGS. Bonds of this class are not subject to tax although they may be bonds of indemnity. A bond filed by order of court to obtain a decree or order for the sale of real estate is a bond given in a legal proceeding and is exempt from tax. Bonds given by court officers under direction or authority of the court, to give proper effect to court proceedings, which bonds are practically a part of the record of a suit or proceeding in court, are not taxable. Bonds given in cases of appeal are not taxable. Bonds given by executors, administrators, guardians and receivers appointed by the court are bonds required in legal proceedings and are not taxable.¹¹

BONDS GIVEN TO STATES AND POLITICAL SUBDIVISIONS THEREOF. Under the former law it was held on the broad ground that the sovereign states and subdivisions

¹¹ T. D. 2091. (Act of October 22, 1914.)

thereof are constitutionally free from taxation by the Federal Government, that bonds given by officials of a state, township, county or village for the faithful performance of duties, were not taxable.¹² Bonds given to a State for the performance of contracts, such as the construction of state or municipal buildings, or the discharge of other duties strictly for or in behalf of the State, when necessary to protect the State's interests, were held not subject to taxation.^{12a} A bond given as a condition to the granting of a license by a State or political subdivision is not taxable if the license is issued in the exercise of the governmental powers of the State or political subdivision.¹³

BONDS GIVEN BY STATES AND POLITICAL SUBDIVISIONS. All bonds given by states, townships, counties and subdivisions thereof are exempt from taxation.¹⁴

BONDS GIVEN TO THE FEDERAL GOVERNMENT. Bonds given to the Federal Government are taxable.¹⁵

BONDS ISSUED IN FOREIGN COUNTRIES. It was held under the former law that bonds issued by guaranty companies in foreign countries guaranteeing the fidelity of individuals or corporations in the United States, executed and delivered in the foreign country, were not taxable, but if they were not valid until countersigned or delivered by the agent in the United States, they should be taxed.¹⁶

BONDS DELIVERED PRIOR TO INCIDENCE OF TAX. Under the

¹² T. D. 2111.

^{12a} T. D. 2072.

¹³ *Ambrosini v. U. S.*, 187 U. S. 1, 23 Sup. Ct. 1, 47 L. Ed. 49.

¹⁴ T. D. 2072.

¹⁵ T. D. 2111.

¹⁶ T. D. 2051.

former law it was held that any bond executed and delivered prior to the date on which the tax was first imposed, whether or not taking effect immediately or subsequent to the enforcement of the taxing act, were not subject to the tax.¹⁷

Building and Loan Associations. Stocks and bonds issued by co-operative building and loan associations which are organized and operated exclusively for the benefit of their members and make loans only to their shareholders, are not subject to the tax.¹⁸ This provision of the law seems to exempt stock of such associations from the tax on original issue and also from the tax on sales or transfers.

Capital Stock, Issue. Although the heading of this paragraph is that used in the statute, the language of the law is that the tax shall be imposed "on each original issue, whether on organization or reorganization, of *certificates of stock* by any association, company or corporation." The rate is five cents on each one hundred dollars of face value or fraction thereof, unless the capital stock is issued without face value, in which case the tax is five cents per share, unless the actual value of the share is in excess of one hundred dollars in which case the tax is five cents on each one hundred dollars of actual value or fraction thereof.¹⁹ The tax is determined by the face value of the certificate.

CONTRACT TO ISSUE STOCK. No stamps are required to

¹⁷ T. D. 2072.

¹⁸ Act of October 3, 1917, Section 801. Under the former law it was held that notes given to or by such associations were taxable. (T. D. 2112.)

¹⁹ The Act of October 22, 1914, was silent as to shares without par value and it was held under that law that such shares were not subject to tax.

be affixed to a contract or agreement by a corporation to issue stock.²⁰ It seems that the tax is on the certificates of stock issued to the shareholders not on the issue of the shares.

ORIGINAL ISSUE OF CERTIFICATES. Under the former law it was held that stock certificates issued in lieu of original certificates in a case where a corporation had changed its name were not taxable as an original issue. Temporary or interim stock certificates issued before the permanent certificates are taxable as original issue; the subsequent exchange of such temporary certificates for the regular stock certificates to the same owner is not subject to any tax.²¹ It was held under the former law that where bonds had been issued with the privilege of exchanging the same for certificates of stock, and the option was exercised after the incidence of the tax, the stock certificates then issued were taxable as an original issue, unless prior to the incidence of the tax the stock certificates in question had been issued and were held in trust for the purchaser of the bonds, in which case the rate of tax on transfers of stock was applicable.²²

STOCK OF FOREIGN CORPORATIONS. Under the former law it was held that certificates of stock sold or delivered within the United States were subject to the same tax as certificates of stock of domestic corporations and under the present law it has been held that stock of a corporation organized in a foreign country issued in the United States is subject to the tax on original issue.

WHERE TO AFFIX STAMPS. The stamps representing the tax imposed on the original issue of stock are required by law to be attached to the stock books and not to the

²⁰ T. D. 2599.

²¹ T. D. 2584.

²² T. D. 2155.

certificates issued.²³ Where the blank stock certificates are not kept in a stock certificate book the stamps should be affixed to the books of record in which the issue of stock is recorded.²⁴

SHARES WITHOUT PAR VALUE. In the case of the issue of certificates of stock without par value it has been held that the value of the share for purpose of taxation will be determined by the statement of the company and the consideration involved in the issue of such stock.²⁵

Capital Stock, Sales and Transfers. The law provides for a tax on (a) all sales, (b) agreements to sell or memoranda of sales or deliveries of or transfers of legal ²⁶ title to shares or certificates of stock in any association, company, or corporation. The tax is imposed whether or not the sale or transfer is shown by the books of the association, company, or corporation, or is made by assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock ²⁷ or not. The rate of tax is two cents on each one hundred dollars of face value or fraction thereof unless the shares of stock are without par value, in which case the rate is 2 cents on each share unless the actual value thereof is in excess of \$100 per share, in which case the tax is 2 cents on each

²³ Act of October 3, 1917, Title 8, Schedule A, Subdivision 3.

²⁴ Letter from Treasury Department dated November 20, 1917.

²⁵ Letter from Treasury Department dated November 26, 1917.

²⁶ The word "legal" was not contained in the Act of October 22, 1914.

²⁷ The Act of October 22, 1914, also read: "or to secure the future payment of money or for the future transfer of any stock."

\$100 of actual value or fraction thereof. The tax is determined by the face value of the certificate of stock, or by the aggregate value of shares without par value represented by the certificate or involved in the sale or transfer. Certain exemptions are expressly made by the language of the law as shown in the following paragraphs.

DEPOSIT OF STOCK CERTIFICATES AS COLLATERAL SECURITY. No tax is intended to be imposed upon an agreement evidencing a deposit of stock certificates as collateral security for money loaned thereon, which certificates are not actually sold, nor upon such stock certificates so deposited. Under the former law it was held that no tax was imposed on stock deposited as collateral until complete title to the certificates of stock was acquired by the pledgee. This seems also to be the rule under the present law.

TRANSFERS TO OR BY A BROKER. No tax is imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased the same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts.²⁸

CERTIFICATE BY BROKER. The following forms have been prescribed for the use of brokers: (a) (in the case of a transfer to a broker) "We hereby certify that we have no ownership, or interest, in * * * shares of the stock above transferred, the transfer by the owner to us being merely for the purpose of sale," (b) (in the case of a transfer by a broker) "We hereby certify that the transfer of * * * of the within shares to the names indicated by the star is made solely to complete the

²⁸ Act of October 3, 1917, Section 807, Schedule A, Subdivision 4.

purchase made by us for our customer, and we have no ownership or interest therein." No broker who has filed a certificate under the foregoing clause (a) of this ruling should file a certificate under the foregoing clause (b) with reference to the transfer of any shares of stock covered by the certificate filed by him under clause (a)²⁹

TRANSFERS TO CLEARING HOUSE. No tax is imposed upon transfers or deliveries to a clearing house for the sole purpose of clearing or adjusting accounts between members, where no beneficial interest is vested in said clearing house or clearing association and there has been no change of title or interest: *Provided*, the exchange, by appropriate by-laws or regulations, requires from its members that all transactions of such members in shares of stock be promptly reported to such clearing house to the end that the stamp taxes thereon may be collected and that no other clearances or settlements or trading in balances are permitted.³⁰

FORMAL TRANSFERS WHERE NO CHANGE OF TITLE TAKES PLACE. The act does not seem to contemplate a tax unless there is a transfer of legal title to the shares or certificates. Hence, it would seem that the following rulings made under the former law would be applicable to the present law: Where a new corporation was formed for the purpose of reorganization the stock certificates of the new company were held subject to tax as original issue but the exchange of certificates of the old company for certificates of the new company to the same person were held not taxable as transfers. In the case of a merger it was held that the exchange of stock of the old companies for stock of the new company resulting from the

²⁹ Regulations 40, Art. 5.

³⁰ Regulations 40, Art. 5.

merger were not subject to the transfer tax. Where upon reorganization new stock was issued to a broker and subsequently transferred by the broker to his customer no tax was imposed upon the transfer. It was also held that preferred stock issued in lieu of common stock was not taxable when there was no change of ownership.

STOCK REDEEMED BY THE ISSUING CORPORATION. Under the former law it was held that where stock was redeemed by a corporation the transfer from the stockholder to the corporation was subject to tax whether or not the stockholder merely surrendered the certificate for cancellation or executed the assignment on the back of the certificate.

LOAN OF CERTIFICATES OF STOCK. Where stock was sold in the regular way but delivery could not be consummated because of non-arrival, and stock was borrowed for the purpose of making delivery, the borrowed stock being subsequently returned to the lender, it was held under the former law that no stamps were required either upon the lending of the certificates or the return of borrowed certificates to the lender. It was required that a certificate should be attached to such transfers to the effect that they were exchanges on account of accommodation loans that in accordance with the ruling of the Treasury Department documentary stamps were not required.³¹

TRANSFERS TO AND BY FIDUCIARIES. Under the former law it was held that transfers from a deceased to his executor or administrator were not taxable. Transfers from a trustee to a substitute trustee were not taxable but transfers from an executor or administrator to a trustee were taxable as were also transfers from the trustee to the beneficiary under the trust. It would seem,

³¹ T. D. 2182.

however, that under the present law transfers of legal title are taxable whether or not the transferee acquires any beneficial interest in the stock.

WHERE TITLE TO THE STOCK PASSED PRIOR TO THE INCIDENCE OF THE TAX. No tax is imposed upon the transfer of such stock on the books of a corporation although made after the date on which the tax was first imposed.³²

TRANSFER OF STOCK BEFORE ISSUE OF CERTIFICATE. The existence of a stock certificate is not essential in order to make the transfer of shares subject to the tax. A transfer affecting a change of ownership of the shares whether made before or after the issuance of the original certificates is taxable.³³ Under the 1914 Law it was held that transfers of subscription warrants entitling the holder to certificates of stock were taxable as transfers of stock.

RIGHTS TO SUBSCRIBE TO STOCK. A right to subscribe to additional stock is neither a share of stock nor a certificate of stock and hence a transfer thereof is not taxable. Under the former law it was held that the transfer of such rights were not taxable.³⁴ Under the present law "rights" are included in the definition of the term "share or shares of stock"^{34a} but it is doubtful if a tax can be legally exacted on transfers of such rights.

SHARES WITHOUT PAR VALUE. The law provides that the tax shall be imposed at the rate of two cents a share unless the actual value of the share is in excess of one hundred dollars, in which case the tax shall be two cents

³² Letter from Treasury Department dated November 30, 1917. This was also the rule under the former law.

³³ T. D. 2599.

³⁴ Letter from Treasury Department dated March 12, 1915.

^{34a} Reg. No. 40, Part 1, Art. 1.

on each one hundred dollars of actual value or fraction thereof. The actual value of shares without par value is determined by the market value at the time of the sale or transfer, which value is considered by the Treasury Department to be the actual value.³⁵

TAX PAID BUT ONCE. Where shares of stock are sold and the tax has been paid and stamps affixed to a bill or memorandum of sale, stamps are not again required when the transfer is made on the books of the company from the name of the party selling to the name of the purchaser.³⁶

MEMORANDUM OF SALES. Every person who makes sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of the legal or beneficial title to shares of stock, at, in or on any exchange or similar place of business, and every person who makes any agreement to sell stock or makes a transfer of stock by delivery of the certificate therefor assigned in blank, shall as a part of every such transaction, promptly make and deliver to the buyer a bill, or memorandum of sale, or agreement to sell, duly signed by the principal or his agent, which shall show the date of the transaction evidenced by it, the names of the seller and buyer, the shares of stock to which it relates, the number of shares and the price per share of said stock, and shall bear a number upon the face thereof. No more than one such bill or memorandum made by the seller on any given day shall bear the same number; *Provided, however,* that no single transaction of a purchase or sale that is made upon an exchange by one member for another member

³⁵ Letter from Treasury Department dated November 26, 1917.

³⁶ T. D. 2073.

shall require to be evidenced by more than one stamped memorandum of sale or agreement to sell.³⁷

STOCK OF FOREIGN CORPORATIONS. When certificates of stock of a foreign corporation are sold or delivered within the United States they are subject to the same tax as certificates of stock of a domestic corporation.³⁸

VOTING TRUST CERTIFICATES. Under the Act of October 22, 1914, it was held that the transfer of the title to stock to voting trustees, the transfer back to the stockholder at the termination of the voting trust, and any and all transfers of the voting trust certificates during the period of the trust were subject to tax as transfers of stock.³⁹ It has also been so ruled under the present law.^{39a}

AFFIXING AND CANCELLATION OF STAMPS. In case the transfer is effected by delivery of the certificate of stock assigned in blank the stamp shall be affixed to the bill, memorandum, or agreement to sell.

In case the change of ownership is by transfer of the certificate of stock, the stamp shall be affixed to the certificate, and in no event shall any company or registrar or transfer agent accept or transfer any shares of stock or certificates therefor unless stamps for all transfer tax required to be affixed to the certificate are attached thereto properly canceled.

In case the evidence of the transfer is shown only by the books of the company the stamp shall be placed upon the books.

In all other cases the payment shall be evidenced by

³⁷ Regulations 40, Art. 6.

³⁸ T. D. 2073.

³⁹ Letter from Treasury Department dated January 7, 1915.

^{39a} Reg. No. 40, Part 1, Art. 1.

affixing the stamp upon the memorandum or agreement of sale to be delivered by the seller to the buyer.

The person using or affixing a stamp shall write or stamp thereon, in ink, his initials, and the day, month, and year on which the same shall be used, or affixed, or shall by cutting or cancelling said stamp with a machine or punch affixing his initials and date as aforesaid, so deface the stamp as to render it unfit for reuse. In addition to the foregoing, stamps of the value of ten cents or more shall have three parallel incisions made by some sharp instrument lengthwise through the stamp after the same has been attached to the bill, memorandum, or other evidence of sale or transfer of stock, provided this will not be required where stamps are canceled by perforation. The cancellation by either method should not so deface the stamp as to prevent its denomination and genuineness from being readily determined.⁴⁰

REGISTRATION OF STOCK BROKERS. Stock brokers, transfer agents and clearing houses are required to register with the collector of internal revenue and to keep records of sales and transfers as more fully set forth in a subsequent part of this chapter.^{40a}

Certificates of Deposit. Certificates of deposit issued by banks and trust companies are not considered to be taxable as certificates of indebtedness, whether or not they are time certificates, or contain a clause reserving the right of thirty days' notice of payment.⁴¹

Certificates of indebtedness. See bonds of indebtedness.

Certificates of Stock. See capital stock.

⁴⁰ Reg. 40, Art. 7.

^{40a} See page 837.

⁴¹ Letter from Terasury Department dated November 16, 1917.

Certificates Generally. No tax is imposed under the present law on certificates of incorporation, certificates of damage, certificates of profit and certificates generally.

Checks. No tax is imposed on checks payable at sight or on demand. Drafts or checks payable otherwise than at sight or on demand are taxable at the same rate as promissory notes. See promissory notes.

Contracts. No tax is imposed by the present law on contracts as such. ⁴²

Conveyances. The law taxes any deed, instrument or writing, whereby any lands, tenements, or other realty *sold* shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction. The tax is based upon the consideration or value of the interest or property conveyed, exclusive of the value of any lien or incumbrance *remaining thereon at the time of sale*. The rate is as follows: When such consideration or value does not exceed one hundred dollars, no tax; exceeding one hundred dollars and not exceeding five hundred dollars, fifty cents; for each additional five hundred dollars or fractional part thereof fifty cents. The tax does not apply to any instrument or writing given to secure a debt.

CONTRACTS TO CONVEY. A contract for the sale of real estate, making provision for future delivery by deed, is not subject to stamp tax. ⁴³

REALTY SOLD. The law provides that deeds whereby any realty sold shall be conveyed to another are taxable. Hence, it seems that if the realty is not sold no stamps need be affixed to the deed. The word "sold" is used

⁴² T. D. 2599.

⁴³ T. D. 2599, T. D. 2115.

in its ordinary meaning and acceptance. There must be a transfer of a valuable interest in the property or payment of a consideration. Thus it has been held under former laws that deeds that are simply confirmatory and do not vest title not already vested are not taxable.⁴⁴ A quit-claim deed given for no consideration, or merely for the nominal consideration of \$1.00, for the purpose of correcting a flaw in title is not subject to tax.⁴⁵ A partition deed which is operated in defining boundary lines or by showing by location the tenant-in-common's interest is not subject to tax.⁴⁶ Deeds of release are exempt from the tax.⁴⁷ Deeds of trust are not subject to the tax.⁴⁸ A deed issued to cover a gift of property from husband to wife or from parent to child, or from an individual to a municipality or other political subdivision, wherein the consideration named is "natural love and affection and \$1.00." "Desire to promote public welfare and \$1.00" or "\$1.00 and other valuable consideration" is not taxable.⁴⁹ If a deed does not grant, assign, transfer, or convey to the purchaser any lands, tenements, or other realty, but only the right to burial, to erect monuments, etc., it does not require a stamp.⁵⁰ Where lands are conveyed by deed to an agent for an undisclosed principal and the property is immediately reconveyed to the principal by the agent, no tax is imposed on the conveyance to the principal if

⁴⁴ Circular No. 503, 2d revision. Compilation of decisions for year 1899, p. 293.

⁴⁵ T. D. 2115.

⁴⁶ T. D. 2115.

⁴⁷ T. D. 2115.

⁴⁸ T. D. 2115.

⁴⁹ T. D. 2115.

⁵⁰ T. D. 19838.

no consideration, or a nominal consideration of \$1.00 only is given. A deed executed by a debtor covering an assignment of property to a trustee to be held for the benefit of creditors is not subject to tax. When, however, the trustee sells or conveys such property either to the creditor, or any other person, the deeds executed by him are taxable.⁵¹ A deed given by a husband and wife to a "straw man" who immediately executes a deed reconveying the property to the husband or the wife is not subject to tax if no valuable consideration, or merely the nominal consideration of \$1.00 is given, and, likewise, the deed of reconveyance is exempt.⁵² A deed transferring title to property to a building and loan association for the purpose of securing a loan on the property so conveyed, which property is immediately reconveyed to its owner is not subject to tax; the deed of reconveyance being likewise exempt.⁵³

MINING DEEDS. Conveyance of a mine located on unpatented land is subject to taxation.⁵⁴ The foregoing ruling was made under the Act of 1898. Under the Act of October 22, 1914, it was held by the Treasury Department in an informal ruling that deeds to mining claims prior to the issue of the patent were taxable upon transfer as conveyances of real property. The tax should be computed upon the interest in the property conveyed which would be the market value of the stock issued therefor, or if it had no market value, the cash value of the mining claim.⁵⁵

PROPERTY IN A FOREIGN COUNTRY. A deed of convey-

⁵¹ T. D. 2115.

⁵² T. D. 2115.

⁵³ T. D. 2115.

⁵⁴ Vol. 1, Treas. Dec. (1899), No. 20986.

⁵⁵ Letter from Treasury Department dated August 3, 1916.

ance conveying real estate that lies in countries that are not United States territory is not subject to taxation, though the grantor and grantee may both be citizens and residents of the United States.⁵⁶

LEASES. Oil leases, leases of mining property, long-term mining leases, etc., which, in themselves, convey no title to, or interest in, real property are exempt from taxation.⁵⁷

OPTIONS. No tax is imposed upon an option for the purchase of real property.⁵⁸

DEEDS GIVEN BY STATES AND POLITICAL SUBDIVISIONS. Deeds executed by a State, county, town or other municipal corporation are not taxable.⁵⁹

DEEDS GIVEN BY OFFICERS OF COURTS. Stamps should be attached to masters' deeds made pursuant to decree of United States District Courts. The execution of the conveyance is not a judicial function, the title to the land being conveyed to the purchaser at the foreclosure sale through the master instead of the defendant himself making the deed. The cost of stamps should be taxed as a part of the costs of the case.⁶⁰

CONSIDERATION OR VALUE. The tax is imposed upon the full amount of consideration or value although payments may have been made upon the installment plan

⁵⁶ Vol. 2, Treas. Dec. (1898), No. 21562. It was also so held under the Act of October 22, 1914.

⁵⁷ T. D. 2155, T. D. 2599.

⁵⁸ T. D. 2115.

⁵⁹ T. D. 2283.

⁶⁰ T. D. 2111, T. D. 2253; *Crawford v. New South Farm & Home Company*, 231 Fed. 999. This case was decided under the Act of October 22, 1914, and it was held that the decision in *Farmers' Loan and Trust Company v. Council Bluffs Gas & Electric Company*, 90 Fed. 806, decided under the Act of June 13, 1898, was applicable.

prior to the incidence of the tax.⁶¹ Quit-claim deeds are taxable according to value of the interest conveyed.⁶² Stock in a corporation is a valuable consideration for the transfer of real property, and a deed conveying real estate to a corporation for such consideration is taxable. The value of the interest in the property conveyed determines the amount of the tax.⁶³ Where a deed states that the transfer is made for a nominal consideration the tax must be computed upon the actual value of the interest or property conveyed.⁶⁴ In a case of an exchange of two properties the deeds transferring title to each are subject to tax, which should, in each case, be computed on the basis of the actual value of the interest or property conveyed (exclusive of the value of any lien or incumbrance remaining thereon at the time of exchange).⁶⁵

INCUMBRANCE ON PROPERTY AT THE TIME OF SALE. The consideration or value on which the tax is based is exclusive of the value of any lien or incumbrance *remaining thereon at the time of sale*. The words in italics were not contained in the former law and it seems were inserted to limit the exclusion to liens or incumbrances other than purchase money mortgages. In determining the amount of incumbrance upon real estate being transferred, no consideration is to be given to new incumbrances placed upon same at the time of, or after, the sale. Only incumbrances which rest on the property before the sale and which are not removed by the sale are to be taken into consideration.^{65a}

⁶¹ T. D. 2279.

⁶² T. D. 20232.

⁶³ T. D. 2278.

⁶⁴ T. D. 2115.

⁶⁵ T. D. 2111, T. D. 2599.

^{65a} T. D. 2599.

WHEN STAMPS AFFIXED. It seems that the stamps should be affixed at the time of delivery of the deed. It was held under the former law that a deed in escrow does not become subject to the tax until the final delivery is made. If such delivery is made subsequent to the incidence of the tax it becomes subject to the tax.⁶⁶ A deed executed and delivered prior to the incidence of the tax is not subject to the tax although recorded after that date.⁶⁷ Deeds delivered after the incidence of the tax must be stamped although they may have been dated, executed and acknowledged prior thereto and even though delivered prior thereto to a third party for account of the grantee named in the deed, if delivery by such party to the grantee is made after the incidence of the tax.⁶⁸

WHO AFFIXES STAMPS. The person who executes the deed (i. e., the grantor) is required to affix the stamps thereto and becomes liable to penalty if stamps in a sufficient amount based upon the actual value of the consideration given are not so affixed.⁶⁹ In a case where the referee at a foreclosure sale did not affix the stamps required by law but the purchaser affixed such stamps under protest before recording the deed, it was held that the grantee, vendee or any other person participating in the making or issuing of a paper without revenue stamps may be required to pay the tax thereon and is liable for failure to do so.⁷⁰

WHERE STAMPS ARE AFFIXED. The stamps should be

⁶⁶ T. D. 2115. So also held in Vol. 2, Treas. Dec. (1898) No. 20096.

⁶⁷ T. D. 2115.

⁶⁸ T. D. 2042.

⁶⁹ T. D. 2115, T. D. 2283.

⁷⁰ T. D. 2310; Home Title Insurance Company v. Keith, 230 Fed. 905.

affixed on the deed or other instrument conveying the real estate.⁷¹

Debentures. See bonds of indebtedness.

Deeds. See conveyances.

Drafts. Drafts drawn at sight or on demand are not taxable. Drafts drawn payable "on arrival of goods" or in any other form than at sight or on demand are subject to the tax if drawn in the United States, unless drawn against exports in which case they are held not to be taxable in view of the constitutional prohibition against tax on exports. Drafts drawn in foreign countries and paid within the United States are not taxable.⁷² The taxability of the draft is determined by the face or form of the instrument and not by any understanding between the maker and the drawee. For rate of tax and rulings regarding taxable drafts see Promissory Notes.

Entry for Withdrawal of Goods or Merchandise from Customs Bonded Warehouse. The tax on instruments of this character is fifty cents. Under the former law it was held that withdrawals for transportation and exportation were not taxable in view of the constitutional provision prohibiting taxation upon exports. It was also held that where entries were filed in duplicate, triplicate, etc., a stamp was required on the original only.⁷³

Entry of Goods, Wares or Merchandise at Custom-house. The law provides that entry of any goods, wares or merchandise at any custom-house, either for consumption or warehousing, shall be taxed as follows:

Not exceeding one hundred dollars in value, twenty-five cents; exceeding one hundred dollars and not exceeding five hundred dollars in value, fifty cents; exceed-

⁷¹ T. D. 2599.

⁷² Letter from Treasury Department dated November 27, 1917.

⁷³ T. D. (Customs) 35040.

ing five hundred dollars in value, one dollar. Under the former law it was held that entries covering merchandise imported solely for governmental purposes were not taxable nor were entries covering merchandise imported for the benefit of foreign ministers, ambassadors or their attaches, even though the entries covering such articles were made by customs brokers.⁷⁴

Interim Certificates. See Capital Stock.

Leases. Leases are not taxed under this law.

Mortgages. Mortgages are not taxed under this law.

Mutual Ditch and Irrigation Companies. Stocks and bonds issued by mutual ditch or irrigation companies are not taxable.⁷⁵ This exemption does not extend to bonds or notes of such companies.

Original Issue of Stock. See Capital Stock, Issue.

Parcels-Post Packages. The tax is imposed upon every parcel or package transported from one point in the United States to another by parcel post on which the postage amounts to twenty-five cents or more. The tax is at the rate of one cent for each twenty-five cents of postage or fractional part thereof. The law requires the tax to be paid by the consignor. It is to be noted that the tax is only on parcels and packages transported from one point to another in the United States. Packages transported to foreign countries are not taxable. Parcels transported from this country to Porto Rico or other possessions are not taxable and packages transported from one point to another in such possessions are not taxable.⁷⁶

Passage Tickets. The tax on passage tickets is only imposed on tickets sold or issued in the United States for

⁷⁴ T. D. (Customs) 35072.

⁷⁵ Act of October 3, 1917, Section 801.

⁷⁶ T. D. 2599.

passage by any vessel to a port or place not in the United States, Canada or Mexico. Such tickets are required to be stamped whether they are one-way or round-trip. No tax is imposed on tickets costing ten dollars or less. The intent seems to be to impose a tax for each passenger based upon the cost of the ticket. The rate is one dollar if the cost of the ticket does not exceed thirty dollars; three dollars if the cost of the ticket exceeds thirty dollars and does not exceed sixty dollars, and five dollars if the cost of the ticket exceeds sixty dollars. Where a single ticket is issued for transportation for more than one passenger the ticket, coupon or prepaid order must be stamped at the proper rate for each passenger based on the number of passengers and the total amount paid for the transportation.⁷⁷ It is the duty of the person selling the ticket to affix and cancel the stamp to the ticket or paper which evidences the sale.⁷⁸ Under former stamp tax laws it has been held that tickets used by members of foreign diplomatic corps were not required to be stamped.⁷⁹

Playing Cards. An additional tax of five cents per pack is imposed upon every pack of playing cards containing not more than fifty-four cards, manufactured or imported, and sold or removed for consumption or sale, after the passage of the act.

Powers of Attorney. Powers of attorney are taxable instruments under this law if they are such that they grant authority to do or perform some act for or in behalf of the grantor, which authority is not otherwise vested in the grantee. The rate of tax is twenty-five cents. The law expressly provides that no stamps shall be re-

⁷⁷ T. D. 2067.

⁷⁸ T. D. 2067.

⁷⁹ Volume 2, Treas. Dec. (1898) No. 20196.

quired on any papers necessary to be used for the collection of claims from the United States or from any State for pensions, back-pay, bounty, or for property lost in the military and naval service. Powers of attorney required in bankruptcy cases are also expressly exempted.

FORMAL POWERS OF ATTORNEY. Powers of attorney which are merely formal and grant no authority which is not otherwise vested in the grantee are not taxable. Thus, it has been held that no tax is imposed upon powers of attorney in the following cases:

ASSIGNMENT OF INSURANCE POLICIES. No stamp tax is imposed upon the power of attorney contained in a transfer by assignment, absolute or as collateral security, of an interest in a contract of insurance, if the power of attorney grants authority to do or perform only such acts for or in behalf of the assignor as are otherwise vested in the assignee.⁸⁰

TO PAY POLL TAXES. Powers of attorney issued in accordance with the provisions of State statutes authorizing a person to pay a poll tax of an individual are not required to be stamped.⁸¹

POWER OF SALE. The power of sale generally embodied in a mortgage, real or chattel, and deed of trust, differs from a power of attorney in many respects, one of which is that the latter always creates an agency or a representative relation, whereas a mortgagee under a power of sale acts on his own behalf and for his own benefit. Such power of sale is not taxable as a power of attorney.⁸²

POWER OF ATTORNEY TO TRANSFER STOCKS. Proforma powers of attorney to transfer stocks or bonds on the

⁸⁰ T. D. 2599.

⁸¹ T. D. 2269.

⁸² T. D. 2196.

books of a corporation given to the purchaser upon the sale or transfer of such stocks or bonds are not taxable.⁸³

POWER OF ATTORNEY GRANTED BY CORPORATION. Where a corporation by resolution of its Board of Directors has empowered an officer thereof to sell, assign or transfer stock or bonds standing in the name of the corporation, or to perform any act in the name of the corporation, such authority is not taxable as power of attorney for the reason that it is necessary for a corporation to perform its corporate acts through one of its officers. If, however, a person other than an officer of the corporation acting in his official capacity is given this authority, the power of attorney so granted would require a twenty-five cent stamp. A general power of attorney granted by a Board of Directors to a person other than an officer of a corporation acting in his official capacity for the purpose of representing the corporation in transactions of a like kind and nature, such as conveying land or acknowledging deeds, is considered by the treasury department as specific authority for each individual transaction, and a revenue stamp is required on each instrument containing the power of attorney.⁸⁴

JUDGMENT NOTES. Where judgment notes contain a clause authorizing any attorney of law to confess judgment in the favor of the holder of the note, such authorization is held not taxable as a power of attorney. The instrument is held to be a warrant of attorney instead of power of attorney.⁸⁵

POWER OF ATTORNEY EXECUTED IN FOREIGN COUNTRY. A power of attorney executed by a person residing in a foreign country to a person in this country is taxable, as

⁸³ T. D. 2085, 2134.

⁸⁴ T. D. 2134.

⁸⁵ Treat v. Tolman, 113 Fed. 892. T. D. 2081.

the instrument is not operative and effective until accepted by the person to whom the power is granted; and, for the same reason, a power of attorney executed by a person residing in this country to a person in a foreign country is not taxable.⁸⁶

WHEN STAMP AFFIXED. The tax on a power of attorney is due when the instrument is executed and is made valid by acceptance, and not when the power is exercised.⁸⁷ A power of attorney containing a power of substitution requires only one twenty-five cent stamp.⁸⁸ A certified copy of a power of attorney, such as is required to be filed on cards in the executive departments of the Government by various insurance and bonding companies, is not taxable.⁸⁹

Produce, Sales of, on Exchange. The tax is imposed upon (a) sales of, (b) agreements of sale, and (c) agreements to sell for future delivery⁹⁰ any products or merchandise at any Exchange or Board of Trade, or other similar place. So-called transferred or scratch sales are expressly included by the statute. No bill, memorandum, agreement or other evidence of a sale, or agreement of sale, or agreement to sell, in case of cash sales of products or merchandise for immediate or prompt delivery which in good faith are actually intended to be delivered are subject to this tax. When the seller of commodities subject to this tax has paid the tax, he may

⁸⁶ T. D. 2134.

⁸⁷ T. D. 2134.

⁸⁸ T. D. 2134.

⁸⁹ T. D. 2134.

⁹⁰ The Act of October 22, 1914, provided for a tax on agreements either for present or for future delivery but made an express exemption to cover cases where products or merchandise were actually delivered at the time of sale or were in vessel, boat or car and actually in the course of transportation.

transfer his contracts to a clearing house without paying a tax on such transfer if the transfer does not vest any beneficial interest in such clearing house association, but is made for the sole purpose of enabling the clearing house association to adjust and balance the accounts of its members on their several contracts. The rate is as follows: Two cents for each one hundred dollars or fraction thereof in value of the merchandise covered by the sale or agreement of sale or agreement to sell.⁹¹

IMMEDIATE OR PROMPT DELIVERY. Cash sales of products or merchandise for immediate or prompt delivery which in good faith are actually intended to be delivered are not taxable. "Immediate or prompt delivery" is held to mean delivery at once or as soon as practicable, and in any event within twenty days from the date of sale or agreement. Every sale or agreement not evidenced by a memorandum or contract expressly requiring immediate or prompt delivery within the above definition is deemed to be for future delivery. In all cases in which the Commissioner is not satisfied from the evidence submitted to him that the transaction was in good faith intended to be followed by immediate or prompt delivery, within the above definition, the seller will be required to pay the tax as on a sale for future delivery.⁹²

EXCHANGE OR BOARD OF TRADE. The law taxes only sales on any exchange or board of trade or other similar place. The word "exchange" is held to mean every agency, auction place, or other meeting place at which produce or merchandise for future delivery is publicly bought, sold, bid for, offered, or exchanged, or contracts for such future delivery are made, either between the

⁹¹ The Act of October 3, 1917, Title 8, Sched. A., Subd. 5.

⁹² Reg. 40, Part 2, Art. 4.

members or patrons of such exchange, or as between members and non-members, patrons, and the public. It includes all incorporated and unincorporated associations of individuals, partnerships, and corporations engaged in the business of publicly selling, buying, or exchanging products or merchandise for future delivery.⁹³

TRANSFERS TO CLEARING HOUSE. Sellers of products, merchandise or commodities having paid the tax provided by law may transfer such contracts to a clearing house association, and such transfer is not taxable within the provisions of the Act, provided that the transfer does not vest any beneficial interest in the clearing house association and is made for the sole purpose of enabling such clearing house association to adjust and balance the accounts of its members on their several contracts. A clearing house is defined to be any incorporated or unincorporated association carried on for the purpose of clearing, settling, and adjusting transactions in purchasing, selling, receiving, or delivering products or merchandise, whether such clearing house be a part or department of an exchange or an independent body.⁹⁴

REGISTRATION AND RECORDS. All persons engaged in the business of making contracts of sale on any exchange and all clearing houses and members of exchanges are required to register and keep records of transactions subject to the tax. The rulings in this respect are referred to more fully in a subsequent part of this chapter.

Promissory Notes. The law provides that the tax on promissory notes, and for each renewal of the same, for a sum not exceeding one hundred dollars shall be two

⁹³ Reg. 40, Part 2, Art. 1.

⁹⁴ Reg. 40, Part 2, Arts. 1 to 4.

cents; and for each additional one hundred dollars or fractional part thereof two cents. The only exception in the statute relates to bank-notes issued for circulation. The law also provides that drafts or checks payable otherwise than at sight or on demand shall be taxed at the same rate.

CHECKS OR DRAFTS PAYABLE OTHERWISE THAN AT SIGHT OR ON DEMAND. Under the former law it was held that in view of the decision made by the Supreme Court of the United States in the case of the United States v. Isham, 17 Wall. 496, that "The liability of an instrument to a stamp duty, as well as the amount of such duty, is determined by the form and face of the instrument, and cannot be effected by proof of facts outside of the instrument itself," drafts, acceptances, overdrafts and postdated checks were not taxable as promissory notes, even though they were used in such a way as to perform some of the functions of a promissory note.⁹⁵ It is no doubt in view of this decision that drafts and checks payable otherwise than at sight or on demand were expressly included in the present law in the same category as promissory notes.

DEFINITION OF PROMISSORY NOTES. Whether or not an instrument is taxable as a promissory note depends upon its form and not upon its use. Thus, a receipt given by a loan company for property received as security for a debt is not a promissory note; but, if in the receipt there is included a promise to pay a certain sum of money at a specified time, with interest, for value received, such a provision in the opinion of the Treasury Department is a valid promissory note, upon which the maker would be liable in a suit at law, and is taxable.⁹⁶ Policy loan and

⁹⁵ T. D. 2170.

⁹⁶ T. D. 2170.

premium extension agreements are not promissory notes as contemplated by the law and therefore are not liable to stamp tax.⁹⁷ In the case of contracts for the purchase of pianos, machinery, and other merchandise, there is sometimes included, among other conditions and provisions, an agreement to pay the vendor a stipulated sum of money at a certain time, with interest, for value received. If this agreement is in form and effect a good and valid promissory note, upon which the maker would be liable in a suit at law, such promissory note is taxable. If, however, the contract merely provides for the payment of the purchase price in installments and enumerates the dates upon which such payments are due, stating, as many of the contracts do, that in default of payment the vendor may take the property, such agreement is not a promissory note.⁹⁸ It is often difficult to make a distinction between promissory notes and bonds of indebtedness. It has been held, however, that the fact that a promissory note is under seal does not make it taxable as a bond.⁹⁹ Nor does the fact that a note may be secured by a mortgage or issued under a deed of trust necessarily make it taxable as a bond. The chief distinction between bonds and promissory notes seems to be the time for which the note or bond is to run. Promises to pay within a comparatively short period of time, such as one year or two years, are usually held to be taxable as notes while promises to pay at the end of a longer period are considered more in the nature of bonds or certificates of indebtedness. Coupon or interest notes attached to and forming part of a bond or principal

⁹⁷ T. D. 2599.

⁹⁸ T. D. 2170.

⁹⁹ T.D. 21815 (Act of June 13, 1898).

note are not subject to tax as promissory notes even though they are in the form of promissory notes.¹⁰⁰

NOTES ISSUED BY FOREIGN GOVERNMENTS. The law provides that no bond, note or other instrument issued by the United States or by any foreign government or by any state, territory, or the District of Columbia or local subdivision thereof, or municipal or other corporation exercising the taxing power, when issued in the exercise of a strictly governmental, taxing, or municipal function shall be subject to tax.¹⁰¹

NOTES DRAWN IN FOREIGN COUNTRIES. A promissory note drawn in a foreign country, and placed in the mails in that country for delivery to a person residing in the United States, is not required to be stamped. Delivery of commercial paper is necessary for its completion and by the weight of authority such an instrument is delivered when placed in the mails. The laws of the foreign country, therefore, would determine the validity of the contract, even if the instrument is made payable in the United States. On the other hand, a promissory note drawn in the United States and placed in the mails for delivery to a person residing in a foreign country is taxable, for the reason above stated.¹⁰²

RENEWAL OF NOTES. A renewal after the incidence of the tax of an instrument issued prior thereto is subject to tax. A written agreement, either attached or detached to a promissory note or in the form of an endorsement on the note, such as "renewed" or "extended" to a certain date, evidencing payment and acceptance of interest in advance to a time certain, sub-

¹⁰⁰ T. D. 2101. *Kenosha v. Lamson*, 9 Wall. 477; *Lexington v. Butler*, 14 Wall. 282.

¹⁰¹ Act of October 3, 1917, Section 801.

¹⁰² T. D. 2170.

sequent to maturity, constitutes a renewal of the note and is subject to tax as such. On the other hand, part payment of a note after it becomes due, or payment of accrued interest after maturity, the note being allowed to run and the holder neither losing or postponing his right of action, is merely in the nature of a forbearance and is not taxable as a renewal.¹⁰³ A contract or agreement extending either a chattel or real estate mortgage is not taxable, but if such extension effects the renewal of promissory notes, either embodied in the mortgage or given in connection with the mortgage, the renewal of such notes is taxable.¹⁰⁴

TRANSFER OF NOTES. No stamp is required upon the transfer by indorsement of promissory notes.

WHO AFFIXES STAMP. The person who makes or issues a promissory note is required by the law to place the stamp upon the same and cancel it. If he does not do so the holder or owner may affix and cancel the stamp as agent for the maker.

Proxies. The tax is imposed on every proxy for voting at any election of officers or for voting at any meeting for the transaction of business of any incorporated company or association. Under the former law the tax was only on proxies for voting at any election of officers. The present law taxes all proxies used at meetings for the transaction of business. The tax is ten cents on each proxy. Proxies for voting at any election of officers, or meeting for the transaction of business of any religious, educational, charitable, fraternal, or literary societies, or public cemeteries, are expressly exempt.

PROXIES SIGNED BY TWO OR MORE STOCKHOLDERS. A

¹⁰³ T. D. 2265.

¹⁰⁴ T. D. 2170.

ten-cent stamp is required for each signature upon a power of attorney or proxy for use in voting at the election of officers of an incorporated company.¹⁰⁵

WHEN STAMPED. It seems that the proxy need not be stamped until it is accepted by the person to whom it is issued but must be stamped before it can be used. Thus, it has been held that a power of attorney or proxy executed by a person residing in a foreign country to a person residing in this country is taxable, as the instrument is not operative and effective until accepted by the person in this country to whom it is issued. Powers of attorney and proxies executed by a person residing in the United States to a person in a foreign country are not taxable.¹⁰⁶ Powers of attorney or proxies executed and accepted before the incidence of the tax are not taxable, even though used after the incidence of the tax.¹⁰⁷

WHO MAY AFFIX STAMPS. Where proxies are sent out by corporations to be executed and returned to the corporation or to the person named in the proxy such proxies may be stamped after execution and delivered by the person receiving the same as the agent of the person executing the proxy.¹⁰⁸ The stamp may be affixed and cancelled either by the party who executes the proxy or by the party to whom the proxy is given.¹⁰⁹ Where the stamp is affixed by an officer or employee of the corporation it is sufficient to cancel the stamp by writing thereon the initials of the officer or employee or the initials of

¹⁰⁵ T. D. 2129.

¹⁰⁶ T. D. 2129.

¹⁰⁷ T. D. 2129.

¹⁰⁸ T. D. 2067.

¹⁰⁹ T. D. 2129.

the corporation and by incision or perforation if the stamp has a value of ten cents or more.¹¹⁰

Rights to Subscribe for Stock. The tax on transfers of stock is imposed upon sales or transfers of legal title to *shares or certificates of stock* in any association, company, or corporation. It was held under the former law that a certificate of right to subscribe for additional stock issued to the stockholders of a corporation was not required to be stamped upon transfer from the stockholder to a third party.¹¹¹ Under the present law it has been ruled that "rights" shall be treated as shares or certificates of stock,^{111a} but this construction does not seem to be supported by the language of the statute.

Security Agreements and Application for Loans. Neither a security agreement signed by a prospective borrower of a bank, empowering the bank to apply any securities, money, or other property of the prospective borrower in the hands of the bank to satisfy the debt of the borrower to the bank, nor the form of application for the loan, is included in the classes of instruments made subject to stamp tax under Schedule A of Section 807, and neither is therefore subject to such tax.¹¹²

Shares Without Par Value. Under the Act of October 22, 1914, shares without par value were not subject to tax either on issue or transfer but under the present law such shares are taxable. See Capital Stock, Issue and Capital Stock, Sales and Transfers, above.

Stock Certificates. See Capital Stock, Issue and Capital Stock, Sales and Transfers, above.

¹¹⁰ Letter from Treasury Department dated January 8, 1915.

¹¹¹ Letter from Treasury Department dated March 12, 1915.

^{111a} Reg. No. 40, Part 1, Art. 1.

¹¹² T. D. 2599.

Transfers of Stock. See Capital Stock, Issue and Capital Stock, Sales and Transfers, above.

Voting Trust Certificates. Voting trust certificates are held to be taxable on transfer as stock certificates. See Capital Stock, Sales and Transfers, above.

Cancellation of Documentary Stamps. Stamps are cancelled by the person using or affixing the stamp, by writing or stamping thereon in ink his initials and the day, month, and year on which the stamp is used or affixed or by cutting or cancelling the stamp with a machine or punch which affixes his initials and date as aforesaid and so defaces the stamp as to render it unfit for reuse. In addition, stamps of the value of ten cents or more are required to be cancelled by three parallel incisions made by some sharp instrument lengthwise through the stamp after the stamp has been attached to the instrument. These parallel incisions, however, are not required where the cancellation is made by perforation. The cancellation by either method should not so deface the stamp as to prevent its denomination and genuineness from being readily determined.¹¹³ When a perforating machine is used it is not necessary that the perforation should outline the initials and date, but it is sufficient if after the initials and date have been written on the stamp, several perforations, sufficient to prevent washing and resale of the stamp are made with an ordinary hand punch before fixing the stamp to the document.¹¹⁴ Where the initials of a person, firm or corporation have been perforated on the stamps before being used it is sufficient when the stamps are actually attached to the document to stamp the same with the

¹¹³ Reg. 40, Part 1, Art. 7.

¹¹⁴ T. D. 2098.

full initials and date. Where the initials of a firm or company have been stamped or written on a stamp it is not required that the individual employee affixing the stamp shall also place his own initials thereon.¹¹⁵

Registration of Stockbrokers and Clearing Houses.

Every person, partnership, corporation, exchange, or clearing house engaged in whole or in part in negotiating, making, or recording sales, agreements to sell, deliveries or transfers of shares or certificates for shares of stock, or in conducting or transacting a stock-brokerage business, or in the clearing, settling, or adjusting of any of the transactions referred to in section 807, subdivision 4 of the act, or who shall be engaged in the business of accepting or procuring the transmission of orders for the sale or purchase or transfers of stock to be made or executed at or under the rules or customs of an exchange in the continental United States, shall, on the first day of December, 1917—and if not on that date engaged in business then within ten days after engaging in business, and on the first day of July annually thereafter—file in the office of the collector of internal revenue of the district in which each place of business of such person, partnership, corporation, exchange, or clearing house is located, or with such other internal-revenue officer as may be hereafter designated, a statement, under oath, setting forth the full name or names of such person or persons, and of all the members of such partnership conducting or transacting the business, with the post-office address or addresses of such person or persons, or partnership, unless the person so certifying be a corporation, exchange, or clearing house, in which event it shall set forth its principal office or place of business,

¹¹⁵ Letter from Treasury Department dated December 9, 1914.

with the names and addresses of its chief officer and secretary, accompanied by a list of its members and their addresses, and if incorporated, when and where incorporated, and if not incorporated under what agreement or authority it is conducting such business or agency. Such statement shall also specifically set forth the character of the business to be conducted, and shall be executed and duly acknowledged by the person or persons so conducting or intending to conduct said business, or by the president or secretary of the corporation or exchange or clearing house. Each exchange or clearing house shall also file with said collector or other designated internal-revenue officer a copy of its constitution, charter, agreement of association, by-laws, rules and regulations, and of all amendments thereto, as the same may from time to time be adopted, and the names and addresses of new members as from time to time admitted to membership.

The said statement shall further contain information as to whether the person executing the same has been licensed under any State laws or under any other provision of Federal law; and if so, the dates and places at which any such licenses were issued. Such statements shall be made upon forms to be furnished upon application to the collector of internal revenue.¹¹⁶

CERTIFICATE OF REGISTRY. Every collector or other designated internal-revenue officer shall file and preserve each statement of registration made to him in accordance with these regulations, and shall issue to such person, partnership, exchange, clearing house, or corporation a certificate of registry, showing the date of issue, the name of the person or persons, or exchange, clearing house, or corporation, conducting the business,

¹¹⁶ Reg. No. 40, Part 1, Art. 2.

the nature of the business for which the license is granted, and the date of expiration of said registry, which certificates shall be signed by the collector or other designated internal-revenue officer, and shall be posted in some prominent place in the office of said person, partnership, exchange, clearing house, or corporation during the period for which issued. If such business is conducted at more than one place, a certificate shall be so posted in each such place of business.¹¹⁷

Record of Sales or Transfers of Stock. All persons who are wholly or partly engaged in the business of buying, selling, or transferring shares of stock, whether at public or private sale, or whether or not they are members of an exchange, including persons engaged in transactions known as "matched," or "on-order," or "pass-outs," or by any other name or term at, on, or in any exchange or similar place, whether or not such transactions are cleared, adjusted, or settled through a clearing house or directly between seller and buyer, or otherwise, shall keep a record showing—

- (a) The date of the transaction.
- (b) The name of the seller or transferor.
- (c) The name of the purchaser or transferee.
- (d) If the order was executed on an exchange, the name of the person who executed the order.
- (e) Whether the transaction is a purchase or sale.
- (f) The name of the corporation the stock of which is the subject of the sale and the number of shares thereof.
- (g) Whether the stock was listed on an exchange.
- (h) Whether the stock was cleared through a clearing house.
- (i) The face or par value of the stock.

(j) The price of the stock if there is no face or par value.

(k) Whether the shares were borrowed or loaned.

(l) Whether the transaction was "matched," "on-order," a "pass-out," or a "scratched sale," or any other kind of sale or purchase.

(m) The amount of tax paid.

(n) The identifying number of the bill or memorandum of sale, as required by article 6 of these regulations.

(o) The origin of the order, whether domestic (referring to the Continental United States), or foreign (referring to other countries).

Persons using such forms may incorporate therein additional columns that would be of use to them, such columns to be placed after the columns containing the information herein required, so as not to interfere with the columns and headings hereby prescribed. These records must be in book form, and all entries therein must be legibly written in ink and the records kept for a period of at least two years. Such record forms will not be supplied by the department.¹¹⁸

Returns of Persons Making Sales of Stock. All persons who are wholly or partly engaged in the business of buying, selling, or transferring shares of stock at, in, or on an exchange, whether or not such sales, purchases, or transfers shall be made, cleared, settled, or adjusted through a clearing house; shall on or before the fifteenth day of each month, and at any other time or times that may be designated by the Commissioner of Internal Revenue, render under oath a true return of all such

¹¹⁸ Reg. No. 40, Part 1, Art. 8. The regulation sets forth in full the form of record required for clearing house transactions and ex-clearing house transactions. Books containing such forms are now supplied by the leading stationers in the large cities.

sales and purchases to said commissioner for the preceding month or for any other period designated by the commissioner, containing in detail the following data and information:

(a) The month for which the return is made.

(b) The name and address of the person, partnership, corporation, or association making the return.

(c) The number of shares of stock sold and purchased on such exchange and cleared by its clearing agency or association.

(d) The number of shares of stock sold and purchased on such exchange that were not cleared by its clearing agency or association.

(e) In respect of shares having a face (or par) value:

(1) The aggregate face value of all shares, not including any fraction of less than \$100 of face value involved in any transaction.

(2) The number of fractions of less than \$100 of face value involved in all transactions.

(f) In respect of shares having no face (or par) value:

(1) As to such shares of an actual value in excess of \$100 per share.

A. The aggregate actual value of all shares, not including any fraction of less than \$100 involved in any transaction.

B. The number of fractions of less than \$100 involved in all transactions in such shares.

(2) As to such shares of an actual value of \$100 or less per share—

A. The total number of such shares.

(g) As to shares purchased, the same information and detail required for shares sold, transferred, and delivered required under (e) and (f) for shares sold, transferred, or delivered.

- (h) The number of shares of stock borrowed.
- (i) The number of shares of stock loaned.
- (j) The number of shares of loaned stock returned.
- (k) The number of shares of borrowed stock returned.
- (l) The amount of tax paid.
- (m) The amount in dollars of stamps purchased during the month.
- (n) The amount in dollars of stamps on hand on the last day of the month for which return is being made.

Such returns shall be made upon forms furnished upon application by the internal revenue collector or other designated officer.

The Commissioner of Internal Revenue may, from time to time, require any person wholly or partly engaged in the business of buying, selling, or transferring shares of stock, whether at public or private sale, and whether or not such sale shall be made on an exchange or cleared, settled, or adjusted through a clearing house to render under oath returns of all such transactions upon forms prescribed by him.¹¹⁹

Returns by Clearing Houses. Every clearing house or committee or body through or by which clearing is done shall, on or before the fifteenth day of each month, and at any other time designated by the Commissioner of Internal Revenue, render in writing under oath to the Commissioner of Internal Revenue a return for the preceding month, or for any other period that may be designated by the commissioner, of all facts in their possession relating to any and all such transactions, and showing in detail:

- (a) The month for which return is made;
- (b) The name and address of the clearing house or

¹¹⁹ Reg. No. 40, Part 1, Art. 9.

similar business, agency, or institution making the return; and

(c) The number of shares of stock directed to be received and the number of shares of stock directed to be delivered and cleared, settled, or adjusted for each member during the month or period for which the return is made.

Such return shall be made upon the forms to be furnished upon application by the collector of internal revenue or other designated officer.

If any person who negotiates sales or transfer of stock on a stock exchange, shall appoint in writing the clearing house for such exchange upon which such sale or transfers are made, if any, his agent for the purposes hereinafter indicated, such clearing house being approved by the Commissioner of Internal Revenue, and shall make a written return, statement or sheet, to such clearing house containing a full disclosure on each business day of all such transactions, both such as are clearable and non-clearable, of the preceding day in shares of stock that are listed or permitted to be dealt in by such member on such exchange, also which if any of such stocks are loaned or borrowed, then in that event such return, statement, or sheet delivered to the clearing house shall be deemed to be the bill, or memorandum of sale, or agreement to sell, required under section 807, subdivision 4, of the act approved October 3, 1917, and such clearing house is hereby authorized to affix to such return, statement, or sheet the amount of stamps required for each sale or agreement to sell or memorandum of sale for delivery or transfer of such stock indicated thereon, and to cancel the stamp so affixed. The affixing and cancellation of such stamps by the clearing house shall be held to be that of the person making such sale or agree-

ment to sell, or memorandum of sale, for delivery or transfer of such stock. The returns, statements, or sheets made to the clearing house shall in respect of each sale show the date thereof, the name of the seller, the name of the buyer, the amount of the sale, and the name of the stock, certificates, voting shares, or other things traded in, but a return for more than one sale may be upon the same return, statement, or sheet, and no settlement of differences or other dealings between members shall be permitted that will interfere with the full disclosure of the whole transaction.

Said clearing house shall preserve the returns, statements, or sheets so made and stamped for at least two years.

But such return, statement, or sheet to the clearing house shall not relieve the person from making the monthly return required by these regulations.

Wherever any clearing house association or similar body carries upon its sheets or records information or reports of transactions showing the transfer by one of its members of an account of a customer without change of ownership of the securities of the customer, there shall be kept by the members of such clearing house or body concerned in such transaction, a record showing the particulars of such transactions.¹²⁰

Substitute Returns—Agents. If any person or clearing house required to make any return by law, or the regulations thereunder, shall fail or refuse to make such return within the time prescribed, such return may be made by an internal revenue officer, upon inspection of the books and papers of the person or clearing house required to make such returns; but the making of such

¹²⁰ Reg. No. 40, Part 1, Art. 10.

return by an internal revenue officer shall not relieve the person or clearing house in default from any penalty incurred by reason of the failure to make such return.

Any officer designated by the Commissioner of Internal Revenue shall have authority to examine the books, papers, and records kept pursuant to these regulations and may require the production of any other books, records, papers, or statements of account, necessary to determine any liability to the tax imposed by the act, or to the observance of the provisions of the regulations made in accordance therewith.¹²¹

Sale of Stamps. No person other than a collector of internal revenue, or duly authorized deputy collector of internal revenue, an Assistant Treasurer, or other United States designated depository shall sell or expose for sale, give away, traffic in, trade, barter, lend, borrow, or exchange any stamp, issued pursuant to these regulations. No person shall buy or receive any such stamps or have the same in his possession or under his control, unless such stamps have been purchased directly from the collector of internal revenue, Assistant Treasurer, or other United States designated depository, in the district in which the stamps are to be used.

All requisitions for stamps to be used under these regulations, shall be made in writing, in ink, on a form prescribed by the Commissioner of Internal Revenue, to the collector of internal revenue, or to an Assistant Treasurer, or other designated depository, in the internal-revenue district in which the stamps are to be used, giving the date thereof, the number and denomination of stamps applied for, and the name and address of the purchaser, and shall be signed in ink by the person receiving the stamps.

¹²¹ Reg. No. 40, Part 1, Art. 11.

The collector of internal revenue to whom such requests are made shall keep a record thereof, and shall keep the requisitions separate and apart from all other requisitions for stamps, and preserve them in his office for a period of two years. Any Assistant Treasurer or designated depository of the United States, receiving requisitions for such stamps shall keep a record of each such requisition and at the end of each month shall file such requisitions with his monthly report to the collector of internal revenue of the district in which said Assistant Treasurer or other designated depository is located.

The stamps to be used under these regulations shall be of such kind and color as are prescribed by the Commissioner of Internal Revenue.¹²²

Registration of Dealers in Futures. Every person engaged in whole or in part in making contracts of sale of any product or merchandise or commodity at, on, or in, or under the rules or customs of any exchange for future delivery or engaged in the business of accepting or procuring the transmission of such contracts of sale, to be executed on any exchange, and every exchange and every clearing house shall, on the first day of December, 1917, and if not on that date engaged in business, then within ten days after engaging in business, and on the first day of July annually thereafter file in the office of the collector of internal revenue of the district in which each place of business of such person, exchange, or clearing house is located, or with such other internal-revenue officer as may be hereafter designated, a statement under oath setting forth the full name of such person, if an individual, and if a partnership the full names of all the members of such partnership, with the post-office address

¹²² Reg. No. 40, Part 1, Art. 12.

of the individual or partnership; and if the person filing such statement be a corporation or association it shall set forth its principal office or place of business with the names and addresses of its chief officer and its secretary, accompanied by a list of its members and their addresses, and if incorporated when and where incorporated, and if unincorporated, under what agreement or authority it is conducting business, together with a copy of such agreement. Statements filed in behalf of any corporation, association, exchange, or clearing house shall be executed and duly acknowledged by the president or secretary thereof. Every statement filed by an exchange or clearing house shall specifically set forth the character of the business conducted or intended to be conducted. Each exchange and clearing house shall also file with the said collector or other designated internal-revenue officer a copy of its constitution, charter, agreement of association, by-laws, and regulations, and all amendments thereto, as the same may from time to time be adopted, and the names and addresses of new members as from time to time admitted to membership.

The statements required by these regulations shall be made upon forms to be prescribed by the Commissioner of Internal Revenue.¹²³

Records and Certificates. Every collector of internal revenue or other designated internal-revenue officer shall file and preserve each statement or registration made to him in accordance with these regulations, and shall issue to the person making such statement a certificate of registry showing the date of issue, the name of the person, the nature of the business for which the certificate is granted, and the date of the expiration of the registra-

tion, which certificate shall be signed by the collector or other designated internal-revenue officer, and shall at all times during the period for which it is issued be posted in some prominent place in the office of the person receiving it. If the business of such person is conducted at more than one place, a certificate shall be so posted in each such place of business.¹²⁴

Records by Sellers and Buyers. All persons who make sales or contracts of sales, including so-called "transferred or scratch sales," "pass outs," "pair-offs," or "matched trades," and all other forms of sale of any product or merchandise at, on, in, or under the rules or customs of any exchange for future delivery shall keep a record showing:

- (a) Date when contract was made.
- (b) Name and address of the other party to the contract.
- (c) Name of person executing the contract.
- (d) Whether the transaction is a purchase or sale.
- (e) Quantity of product, merchandise, or commodity involved; whether in tons, pounds, bales, bushels, bags, mats, barrels, gallons, or other unit of measure or weight, as the case may be.
- (f) Name of product, merchandise, or commodity, including (if not a basis grade contract) grade, type, sample, or description.
- (g) Name of customer.
- (h) Whether the contract is a "basis grade" contract.
- (i) Time specified in contract for delivery.
- (j) Specified price per ton, pound, mat, bale, bag,

¹²⁴ Reg. No. 40, Part 2, Art. 3.

bushel, barrel, gallon, or other unit of measure or weight, as the case may be.

(k) Gross amount of sale or purchase.

(l) Amount of tax paid.

(m) Whether the order for sale or purchase was of domestic (meaning the continental United States) or foreign origin (meaning from countries other than the continental United States).

(n) Date of delivery or settlement.

(o) Method of fulfillment or settlement.

Persons who use such forms may incorporate additional columns which would be of use to them, such columns to be placed in such positions as not to interfere with the columns and headings prescribed. Such record forms will not be supplied by the department.^{124a}

The records required by these regulations shall be legibly written in ink and kept separate in books, and contracts of sale for future delivery of two or more distinct products or merchandise shall be kept separate. Any person who executes or makes such contracts of sale shall preserve the trading cards, memoranda, or slips of each transaction, and the purchaser shall preserve the bill, memorandum, or evidence of sale to which the stamps are affixed, for the period of two years.¹²⁵

Records to Be Kept by Clearing Houses. All persons who act in the capacity of a clearing house or clearing association shall keep a record showing:

(a) Name of person for whom each contract is cleared.

(b) Date when contract was made.

(c) Whether the transaction is a purchase or sale.

^{124a} The regulation sets forth in full the form of record required. Books containing such forms are now supplied by the leading stationers in the large cities.

¹²⁵ Reg. No. 40, Part 2, Art. 6.

(d) Quantity of product, merchandise, or commodity involved, whether in tons, pounds, bales, bushels, bags, mats, barrels, gallons, or other unit of measure or weight, as the case may be.

(e) Name of product, merchandise, or commodity, including (if not a basis-grade contract) grade, type, sample, or description.

(f) Whether the contract is a basis-grade contract.

(g) Time specified in contract for delivery.

(h) Date of settlement.

(i) Method of settlement.

Records of sales for future delivery of two or more distinct products or merchandise must be kept separate.¹²⁶

Returns by Members of Exchanges. All persons who make contracts of sale of any commodity, product, or merchandise, at, on, or in any exchange, board of trade, or other similar place of business, for future delivery, whether such contracts shall be cleared and adjusted through a clearing house, or clearing association, or directly between the seller and buyer, or otherwise, shall on or before the fifteenth day of each month, and at any other time required by the Commissioner of Internal Revenue, make return, in writing, to the Commissioner of Internal Revenue, or some officer designated by him, for the preceding month or any other period, verified before some officer authorized to administer oaths, showing:

(a) The number of contracts of sale and purchase of each product, merchandise, or commodity brought forward from the preceding month.

(b) The number of contracts of sale and purchase of each product, merchandise, or commodity during the current month.

¹²⁶ Reg. No. 40, Part 2, Art. 7.

(c) The month in which the products, merchandise, or commodity is to be delivered.

(d) The method of settlement of each contract, i. e., whether by "actual delivery," "notice," "ring," "direct," "transfer," or "scratch sale," "pair off," or "matched," "pass out," "set-off," "give up," through a clearing house or clearing association, or otherwise.

(e) The gross amount of the contracts of sale.

(f) The tax paid thereon.

(g) The number of contracts both of purchase and sale left open at the end of the month.

(h) The amount of stamps on hand from preceding month.

(i) The amount of stamps purchased during month.

(j) The amount of stamps used during month.

(k) Balance of stamps on hand at end of month.

(l) The origin of the order of the contracts, whether domestic or foreign.

Such returns shall be made upon forms to be furnished, upon application, by the collector of internal revenue, or other designated officer of the district in which the exchange, board of trade, or other similar place is located.¹²⁷

Returns by Clearing Houses. Every clearing house, or clearing association, shall on or before the 15th day of each month, and at any other time required, render in writing, under oath, a return, for the preceding month or for any other period designated, to the Commissioner of Internal Revenue of all facts in their possession showing:

(a) The number of contracts "long" and "short" for each member brought forward from the preceding month.

¹²⁷ Reg. No. 40, Part 2, Art. 8.

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(b) The number of contracts bought or sold by each member of the association.

(c) The number of tons, pounds, bales, bushels, bags, mats, barrels, or gallons, or other units of weight or measure involved in such contracts, as the case may be.

(d) The month in which such product, merchandise, or commodity is to be delivered.

(e) The method of settlement of said contracts—i. e., whether by “set-off,” “notice,” or “delivery,” or by any other method.

(f) The number of open contracts “long” and “short” for each member carried to the following month.

Such returns shall be made upon forms to be furnished, upon application, by the collector of internal revenue of the district, or other designated officer, in which the clearing house or clearing association is situated.¹²⁸

Failure to Make Returns. If any person, or clearing house or clearing association, required to make returns by this act, or the regulations thereunder, shall fail or refuse to make any return within the time prescribed in these regulations, or designated by the Commissioner of Internal Revenue, then the same shall be made by an internal revenue officer, upon inspection of the books and papers of the person, or clearing house, or clearing association, so required; but the making of said return by an internal-revenue officer shall not relieve the person in default from any penalty incurred by reason of his failure to make such return.

Any officer designated by the Commissioner of Internal Revenue shall have authority to examine the books, papers, and records kept pursuant to these regulations, and may require the production of any other books, records,

¹²⁸ Reg. No. 40, Part 2, Art. 9.

papers, or statements of account, necessary to determine any liability to the tax imposed by this act, or the observance of the provisions of the regulations made in accordance therewith.¹²⁹

Sale of Stamps. No person other than a collector of internal revenue, or duly authorized deputy collector of internal revenue, assistant treasurer, or designated depository of the United States, in the district in which is located an exchange, shall sell or expose for sale, traffic in, trade, barter, or exchange any stamp required by law or by these regulations to be used for the payment of taxes upon sales or contracts of sale of any product or merchandise in future delivery.

All requisitions for such stamps shall be made in writing on a form prescribed by the Commissioner of Internal Revenue, to the collector of internal revenue, an assistant treasurer, or designated depository in the internal-revenue district in which the stamps are to be used, giving the date thereof, the number and denomination of stamps applied for, and the name and address of the purchaser, and shall be signed in ink by the person receiving the stamps. If the requisition for such stamps shall be made to any assistant treasurer or designated depository of the United States, such assistant treasurer or designated depository shall keep a record thereof, and at the end of each month shall file such requisitions with his monthly report with the collector of internal revenue of the district in which said assistant treasurer or designated depository is located. The collector of internal revenue shall keep the requisitions for such stamps made to him and those filed by such assistant treasurer or designated depository separate and apart from all other requisitions

¹²⁹ Reg. No. 40, Part 2, Art. 10.

for stamps and preserve them in his office for a period of two years.

The stamps shall be of a color and design prescribed by the Commissioner of Internal Revenue.¹³⁰

Penalties. The present law contains no provision that an unstamped instrument shall be void or shall not be admitted as evidence in the courts or shall not be placed on record. Anyone who makes, signs, issues or accepts an instrument without the tax being paid or consigns or ships an article without the tax being paid or manufactures or imports or sells playing cards without the tax being paid or makes use of a stamp without canceling or obliterating the same is guilty of a misdemeanor punishable by a fine of not more than one hundred dollars for each offense. The penalty for fraudulent removal or reuse of a stamp or having possession of washed, restored or altered stamps removed from any instrument is a fine of not more than one thousand dollars or imprisonment for not more than five years or both, at the discretion of the court.¹³¹

¹³⁰ Reg. No. 40, Part 2, Art. 11.

¹³¹ Act of October 3, 1917, Sections 802 and 803.

TEXT OF WAR EXCESS PROFITS TAX LAW

TITLE II OF THE ACT OF OCTOBER 3, 1917

Sec. 200. That when used in this title—

The term “corporation” includes joint-stock companies or associations, and insurance companies;

The term “domestic” means created under the law of the United States, or of any State, Territory or District thereof, and the term “foreign” means created under the law of any other possession of the United States or of any foreign country or government;

The term “United States” means only the States, the Territories of Alaska and Hawaii, and the District of Columbia;

The term “taxable year” means the twelve months ending December thirty-first, excepting in the case of a corporation or partnership which has fixed its own fiscal year, in which case it means such fiscal year. The first taxable year shall be the year ending December thirty-first, nineteen hundred and seventeen, except that in the case of a corporation or partnership which has fixed its own fiscal year, it shall be the fiscal year ending during the calendar year nineteen hundred and seventeen. If a corporation or partnership, prior to March first, nineteen hundred and eighteen, makes a return covering its own fiscal year, and includes therein the income received during that part of the fiscal year falling within the calendar year nineteen hundred and sixteen, the tax for such taxable year shall be that proportion of the tax computed upon the net income during such fiscal year which the time from January first, nineteen hundred and seventeen, to the end of such fiscal year bears to the full fiscal year; and

The term “prewar period” means the calendar years nineteen hundred and eleven, nineteen hundred and twelve, and nineteen hundred and thirteen, or, if a corporation or partnership was not in existence or an individual was not engaged in a trade or business during the whole of such period, then as many of such years dur-

ing the whole of which the corporation or partnership was in existence or the individual was engaged in the trade or business.

The terms 'trade' and 'business' include professions and occupations.

The term "net income" means in the case of a foreign corporation or partnership or a non-resident alien individual, the net income received from sources within the United States.

Sec. 201. That in addition to the taxes under existing law and under this Act there shall be levied, assessed, collected, and paid for each taxable year upon the income of every corporation, partnership, or individual, a tax (hereinafter in this title referred to as the tax) equal to the following percentages of the net income:

Twenty per centum of the amount of the net income in excess of the deduction (determined as hereinafter provided) and not in excess of fifteen per centum of the invested capital for the taxable year;

Twenty-five per centum of the amount of the net income in excess of fifteen per centum and not in excess of twenty per centum of such capital;

Thirty-five per centum of the amount of the net income in excess of twenty per centum and not in excess of twenty-five per centum of such capital;

Forty-five per centum of the amount of the net income in excess of twenty-five per centum and not in excess of thirty-three per centum of such capital; and

Sixty per centum of the amount of the net income in excess of thirty-three per centum of such capital.

For the purpose of this title every corporation or partnership not exempt under the provisions of this section shall be deemed to be engaged in business, and all the trades and businesses in which it is engaged shall be treated as a single trade or business, and all its income from whatever source derived shall be deemed to be received from such trade or business.

This title shall apply to all trades or businesses of whatever description, whether continuously carried on or not, except—

(a) In the case of officers and employees under the United States, or any State, territory, or the District of Columbia, or any local sub-division thereof, the compensation or fees received by them as such officers or employees;

(b) Corporations exempt from tax under the provisions of section eleven of Title I of such act of September eighth, nineteen

hundred and sixteen, as amended by this Act, and partnerships and individuals carrying on or doing the same business, or coming within the same description; and

(c) Incomes derived from the business of life, health, and accident insurance combined in one policy issued on the weekly premium payment plan.

Sec. 202. That the tax shall not be imposed in the case of the trade or business of a foreign corporation or partnership or a non-resident alien individual, the net income of which trade or business during the taxable year is less than \$3,000.

Sec. 203. That for the purposes of this title the deduction shall be as follows, except as otherwise in this title provided—

(a) In the case of a domestic corporation, the sum of (1) an amount equal to the same percentage of the invested capital for the taxable year which the average amount of the annual net income of the trade or business during the prewar period was of the invested capital for the prewar period (but not less than seven or more than nine per centum of the invested capital for the taxable year), and (2) \$3,000;

(b) In the case of a domestic partnership or of a citizen or resident of the United States, the sum of (1) an amount equal to the same percentage of the invested capital for the taxable year which the average amount of the annual net income of the trade or business during the prewar period was of the invested capital for the prewar period (but not less than seven or more than nine per centum of the invested capital for the taxable year), and (2) \$6,000;

(c) In the case of a foreign corporation or partnership or of a nonresident alien individual, an amount ascertained in the same manner as provided in subdivisions (a) and (b), without any exemption of \$3,000 or \$6,000.

(d) If the Secretary of the Treasury is unable satisfactorily to determine the average amount of the annual net income of the trade or business during the prewar period, the deduction shall be determined in the same manner as provided in section two hundred and five.

Sec. 204. That if a corporation or partnership was not in existence, or an individual was not engaged in the trade or business, during the whole of any one calendar year during the prewar period, the deduction shall be an amount equal to eight per centum of the invested capital for the taxable year, plus in the case of

a domestic corporation \$3,000, and in the case of a domestic partnership or a citizen or resident of the United States \$6,000.

A trade or business carried on by a corporation, partnership, or individual, although formally organized or reorganized on or after January second, nineteen hundred and thirteen, which is substantially a continuation of a trade or business carried on prior to that date, shall, for the purposes of this title, be deemed to have been in existence prior to that date, and the net income and invested capital of its predecessor prior to that date shall be deemed to have been its net income and invested capital.

Sec. 205. (a) That if the Secretary of the Treasury, upon complaint finds either (1) that during the prewar period a domestic corporation or partnership, or a citizen or resident of the United States, had no net income from the trade or business, or (2) that during the prewar period the percentage, which the net income was of the invested capital, was low as compared with the percentage, which the net income during such period of representative corporations, partnerships, and individuals, engaged in a like or similar trade or business, was of their invested capital, then the deduction shall be the sum of (1) an amount equal to the same percentage of its invested capital for the taxable year which the average deduction (determined in the same manner as provided in section two hundred and three, without including the \$3,000 or \$6,000 therein referred to) for such year of representative corporations, partnerships or individuals, engaged in a like or similar trade or business, is of their average invested capital for such year, plus (2) in the case of a domestic corporation \$3,000, and in the case of a domestic partnership or a citizen or resident of the United States \$6,000.

The percentage which the net income was of the invested capital in each trade or business shall be determined by the Commissioner of Internal Revenue, in accordance with the regulations prescribed by him, with the approval of the Secretary of the Treasury. In the case of a corporation or partnership which has fixed its own fiscal year, the percentage determined by the calendar year ending during such fiscal year shall be used.

(b) The tax shall be assessed upon the basis of the deduction determined as provided in section two hundred and three, but the taxpayer claiming the benefit of this section may at the time of making the return file a claim for abatement of the amount by which the tax so assessed exceeds a tax computed upon the basis

of the deduction determined as provided in this section. In such event, collection of the part of the tax covered by such claim for abatement shall not be made until the claim is decided, but if in the judgment of the Commissioner of Internal Revenue, the interests of the United States would be jeopardized thereby he may require the claimant to give a bond in such amount and with such sureties as the Commissioner may think wise to safeguard such interests, conditioned for the payment of any tax found to be due, with the interest thereon, and if such bond, satisfactory to the Commissioner, is not given within such time as he prescribes, the full amount of the tax assessed shall be collected and the amount overpaid, if any, shall upon final decision of the application be refunded as a tax erroneously or illegally collected.

Sec. 206. That for the purposes of this title the net income of a corporation shall be ascertained and returned (a) for the calendar years nineteen hundred and eleven and nineteen hundred and twelve upon the same basis and in the same manner as provided in section thirty-eight of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes," approved August fifth, nineteen hundred and nine, except that income taxes paid by it within the year imposed by the authority of the United States shall be included; (b) for the calendar year nineteen hundred and thirteen upon the same basis and in the same manner as provided in section II of the Act entitled "An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes," approved October third, nineteen hundred and thirteen, except that income taxes paid by it within the year imposed by the authority of the United States shall be included, and except that the amounts received by it as dividends upon the stock or from the net earnings of other corporations, joint-stock companies or associations, or insurance companies, subject to the tax imposed by section II of such Act of October third, nineteen hundred and thirteen, shall be deducted; and (c) for the taxable year upon the same basis and in the same manner as provided in Title I of the Act entitled "An Act to increase the revenue, and for other purposes," approved September eighth, nineteen hundred and sixteen, as amended by this Act, except that the amounts received by it as dividends upon the stock or from the net earnings of other corporations, joint-stock companies or associations, or insurance companies, subject to the tax imposed by Title I of such Act of

September eighth, nineteen hundred and sixteen, shall be deducted.

The net income of a partnership or individual shall be ascertained and returned for the calendar years nineteen hundred and eleven, nineteen hundred and twelve, and nineteen hundred and thirteen, and for the taxable year, upon the same basis and in the same manner as provided in Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, except that the credit allowed by subdivision (b) of section five of such Act shall be deducted. There shall be allowed (a) in the case of a domestic partnership the same deductions as allowed to individuals in subdivision (a) of section five of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act; and (b) in the case of a foreign partnership the same deductions as allowable to individuals in subdivision (a) of section six of such Act as amended by this Act.

Sec. 207. That as used in this title the term "invested capital" for any year means the average invested capital for the year, as defined and limited in this title, averaged monthly.

As used in this title "invested capital" does not include stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to the tax imposed by this title, nor money or other property borrowed, and means, subject to the above limitations:

(a) In the case of a corporation or partnership: (1) actual cash paid in, (2) the actual cash value of tangible property paid in other than cash, for stock or shares in such corporation or partnership, at the time of such payment (but in case such tangible property was paid in prior to January first, nineteen hundred and fourteen, the actual cash value of such property as of January first, nineteen hundred and fourteen, but in no case to exceed the par value of the original stock or shares specifically issued therefor), and (3) paid in or earned surplus and undivided profits used or employed in the business, exclusive of undivided profits earned during the taxable year; *Provided*, That (a) the actual cash value of patents and copyrights paid in for stock or shares in such corporation or partnership, at the time of such payment, shall be included as invested capital, but not to exceed the par value of such stock or shares at the time of such payment, and (b) the good will, trade marks, trade brands, the franchise of a corporation or partnership, or other intangible property, shall be included as invested capital if the corporation or partnership made payment

bona fide therefor specifically as such in cash or tangible property, the value of such good will, trade mark, trade brand, franchise, or intangible property, not to exceed the actual cash or actual cash value of the tangible property paid therefor at the time of such payment; but good will, trade marks, trade brands, franchise of a corporation or partnership, or other intangible property, bona fide purchased, prior to March third, nineteen hundred and seventeen, for and with interests or shares in a partnership or for and with shares in the capital stock of a corporation (issued prior to March third, nineteen hundred and seventeen), in an amount not to exceed, on March third, nineteen hundred and seventeen, twenty per centum of the total interests or shares in the partnership or of the total shares of the capital stock of the corporation, shall be included in invested capital at a value not to exceed the actual cash value at the time of such purchase, and in case of issue of stock therefor not to exceed the par value of such stock;

(b) In the case of an individual, (1) actual cash paid into the trade or business, and (2) the actual cash value of tangible property paid into the trade or business, other than cash, at the time of such payment (but in case such tangible property was paid in prior to January first, nineteen hundred and fourteen, the actual cash value of such property as of January first, nineteen hundred and fourteen), and (3) the actual cash value of patents, copyrights, good will, trade marks, trade brands, franchises, or other intangible property, paid into the trade or business, at the time of such payment, if payment was made therefor specifically as such in cash or tangible property, not to exceed the actual cash or actual cash value of the tangible property bona fide paid therefor at the time of such payment.

In the case of a foreign corporation or partnership or of a non-resident alien individual the term "invested capital" means that proportion of the entire invested capital, as defined and limited in this title, which the net income from sources within the United States bears to the entire net income.

Sec. 208. That in case of the reorganization, consolidation, or change of ownership of a trade or business after March third, nineteen hundred and seventeen, if an interest or control in such trade or business of fifty per centum or more remains in control of the same persons, corporations, associations, partnerships, or any of them, then in ascertaining the invested capital of the trade or business no asset transferred or received from the prior trade or

business shall be allowed a greater value than would have been allowed under this title in computing the invested capital of such prior trade or business if such asset had not been so transferred or received, unless such asset was paid for specifically as such, in cash or tangible property, and then not to exceed the actual cash or actual cash value of the tangible property paid therefor at the time of such payment.

Sec. 209. That in the case of a trade or business having no invested capital or not more than a nominal capital there shall be levied, assessed, collected and paid, in addition to the taxes under existing law and under this act, in lieu of the tax imposed by section two hundred and one, a tax equivalent to eight per centum of the net income of such trade or business, in excess of the following deductions: in the case of a domestic corporation, \$3,000, and in the case of a domestic partnership or a citizen or resident of the United States, \$6,000; in the case of all other trades or business, no deduction.

Sec. 210. That if the Secretary of the Treasury is unable in any case satisfactorily to determine the invested capital, the amount of the deduction shall be the sum of (1) an amount equal to the same proportion of the net income of the trade or business received during the taxable year as the proportion which the average deduction (determined in the same manner as provided in section two hundred and three, without including the \$3,000 or \$6,000 therein referred to) for the same calendar year of representative corporations, partnerships, and individuals, engaged in a like or similar trade or business, bears to the total net income of the trade or business received by such corporations, partnerships, and individuals, plus (2) in the case of a domestic corporation \$3,000, and in the case of a domestic partnership or a citizen or resident of the United States \$6,000.

For the purpose of this section the proportion between the deduction and the net income in each trade or business shall be determined by the Commissioner of Internal Revenue in accordance with regulations prescribed by him, with the approval of the Secretary of the Treasury. In the case of a corporation or partnership which has fixed its own fiscal year, the proportion determined for the calendar year ending during such fiscal year shall be used.

Sec. 211. That every foreign partnership having a net income of \$3,000 or more for the taxable year, and every domestic part-

nership having a net income of \$6,000 or more for the taxable year, shall render a correct return of the income of the trade or business for the taxable year, setting forth specifically the gross income for such year, and the deductions allowed in this title. Such returns shall be rendered at the same time and in the same manner as is prescribed for income-tax returns under Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act.

Sec. 212. That all administrative, special, and general provisions of law, including the laws in relation to the assessment, remission, collection, and refund of internal-revenue taxes not heretofore specifically repealed, and not inconsistent with the provisions of this title, are hereby extended and made applicable to all the provisions of this title and to the tax herein imposed, and all provisions of Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, relating to returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this title.

Sec. 213. That the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, shall make all necessary regulations for carrying out the provisions of this title, and may require any corporation, partnership, or individual, subject to the provisions of this title, to furnish him with such facts, data, and information as in his judgment are necessary to collect the tax imposed by this title.

Sec. 214. That Title II (sections two hundred to two hundred and seven, inclusive) of the Act entitled "An Act to provide increased revenue to defray the expenses of the increased appropriations for the Army and Navy, and the extensions of fortifications, and for other purposes," approved March third, nineteen hundred and seventeen, is hereby repealed.

Any amount heretofore or hereafter paid on account of the tax imposed by such Title II, shall be credited toward the payment of the tax imposed by this title, and if the amount so paid exceeds the amount of such tax the excess shall be refunded as a tax erroneously or illegally collected.

Subdivision (1) of section three hundred and one of such Act of September eighth, nineteen hundred and sixteen, is hereby amended so that the rate of tax for the taxable year nineteen hundred and seventeen shall be ten per centum instead of twelve and one-half per centum, as therein provided.

Subdivision (2) of such section is hereby amended to read as follows:

“(2) This section shall cease to be of effect on and after January first, nineteen hundred and eighteen.”

TEXT OF WAR STAMP TAX LAW

TITLE VIII OF THE ACT OF OCTOBER 3, 1917

Sec. 800. That on and after the first day of December, nineteen hundred and seventeen, there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters and things mentioned and described in Schedule A of this title, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, by any person, corporation, partnership, or association who makes, signs, issues, sells, removes, consigns, or ships the same, or for whose use or benefit the same are made, signed, issued, sold, removed, consigned, or shipped, the several taxes specified in such schedule.

Sec. 801. That there shall not be taxed under this title any bond, note, or other instrument, issued by the United States, or by any foreign Government, or by any State, Territory, or the District of Columbia, or local subdivision thereof, or municipal or other corporation exercising the taxing power, when issued in the exercise of a strictly governmental, taxing, or municipal function; or stock and bonds issued by co-operative building and loan associations which are organized and operated exclusively for the benefit of their members and make loans only to their shareholders, or by mutual ditch or irrigating companies.

Sec. 802. That whoever—

(a) Makes, signs, issues or accepts, or causes to be made, signed, issued, or accepted, any instrument, document, or paper of any kind or description whatsoever without the full amount of tax thereon being duly paid;

(b) Consigns or ships, or causes to be consigned or shipped, by parcel post any parcel, package or article without the full amount of tax being duly paid;

(c) Manufactures or imports and sells, or offers for sale, or causes to be manufactured or imported and sold, or offered for

sale, any playing cards, package, or other article without the full amount of tax being duly paid;

(d) Makes use of an adhesive stamp to denote any tax imposed by this title without canceling or obliterating such stamp as prescribed in section eight hundred and four;

Is guilty of a misdemeanor and upon conviction thereof shall pay a fine of not more than \$100 for each offense.

Sec. 803. That whoever—

(a) Fraudulently cuts, tears, or removes from any vellum, parchment, paper, instrument, writing, package, or article, upon which any tax is imposed by this title, any adhesive stamp or the impression of any stamp, die, plate, or other article provided, made, or used in pursuance of this title; (b) Fraudulently uses, joins, fixes, or places to, with, or upon any vellum, parchment, paper, instrument, writing, package, or article, upon which any tax is imposed by this title, (1) any adhesive stamp, or the impression of any stamp, die, plate, or other article, which has been cut, torn, or removed from any other vellum, parchment, paper, instrument, writing, package, or article, upon which any tax is imposed by this title or (2) any adhesive stamp or the impression of any stamp, die, plate, or other article of insufficient value; or (3) any forged or counterfeit stamp, or the impression of any forged or counterfeited stamp, die, plate, or other article;

(c) Willfully removes, or alters the cancellation, or defacing marks of, or otherwise prepares, any adhesive stamp, with intent to use, or cause the same to be used, after it has been already used, or knowingly or willfully buys, sells, offers for sale, or gives away, any such washed or restored stamp to any person for use, or knowingly uses the same;

(d) Knowingly and without lawful excuse (the burden of proof of such excuse being on the accused) has in possession any washed, restored, or altered stamp, which has been removed from any vellum, parchment, paper, instrument, writing, package, or article,

is guilty of a misdemeanor, and upon conviction shall be punished by a fine of not more than \$1,000, or by imprisonment for not more than five years, or both, in the discretion of the court, and any such reused, canceled, or counterfeit stamp and the vellum, parchment, document, paper, package, or article upon which it is placed or impressed shall be forfeited to the United States.

Sec. 804. That whenever an adhesive stamp is used for denot-

ing any tax imposed by this title, except as hereinafter provided, the person, corporation, partnership, or association using or affixing the same shall write or stamp or cause to be written or stamped thereupon the initials of his or its name and the date upon which the same is attached or used, so that the same may not again be used: *Provided*, That the Commissioner of Internal Revenue may prescribe such other method for the cancellation of such stamps as he may deem expedient.

Sec. 805. (a) That the Commissioner of Internal Revenue shall cause to be prepared and distributed for the payment of the taxes prescribed in this title suitable stamps denoting the tax on the document, articles, or thing to which the same may be affixed, and shall prescribe such method for the affixing of said stamps in substitution for or in addition to the method provided in this title, as he may deem expedient.

(b) The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, is authorized to procure any of the stamps provided for in this title by contract whenever such stamps cannot be speedily prepared by the Bureau of Engraving and Printing; but this authority shall expire on the first day of January, nineteen hundred and eighteen, except as to imprinted stamps furnished under contract, authorized by the Commissioner of Internal Revenue.

(c) All internal-revenue laws relating to the assessment and collection of taxes are hereby extended to and made a part of this title, so far as applicable, for the purpose of collecting stamp taxes omitted through mistake or fraud from any instrument, document, paper, writing, parcel, package, or article named herein.

Sec. 806. That the Commissioner of Internal Revenue shall furnish to the Postmaster General without prepayment a suitable quantity of adhesive stamps to be distributed to and kept on sale by the various postmasters in the United States. The Postmaster General may require each such postmaster to give additional or increased bond as postmaster for the value of the stamps so furnished, and each such postmaster shall deposit the receipts from the sale of such stamps to the credit of and render accounts to the Postmaster General at such times and in such form as he may by regulations prescribe. The Postmaster General shall at least once monthly transfer all collections from this source to the Treasury as internal-revenue collections.

Sec. 807. That the collectors of the several districts shall furnish.
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nish without prepayment to any assistant treasurer or designated depository of the United States located in their respective collection districts a suitable quantity of adhesive stamps for sale. In such cases the collector may require a bond, with sufficient sureties, to an amount equal to the value of the adhesive stamps so furnished, conditioned for the faithful return, whenever so required, of all quantities or amounts undisposed of, and for the payment monthly of all quantities or amounts sold or not remaining on hand. The Secretary of the Treasury may from time to time make such regulations as he may find necessary to insure the safe-keeping or prevent the illegal use of all such adhesive stamps.

SCHEDULE A—Stamp Taxes

1. Bonds of indebtedness: Bonds, debentures, or certificates of indebtedness issued on and after the first day of December, nineteen hundred and seventeen, by any person, corporation, partnership, or association, on each \$100 of face value or fraction thereof, 5 cents: *Provided*, That every renewal of the foregoing shall be taxed as a new issue: *Provided further*, That when a bond conditioned for the repayment or payment of money is given in a penal sum greater than the debt secured, the tax shall be based upon the amount secured.

2. Bonds, indemnity, and surety: Bonds for indemnifying any person, corporation, partnership, or corporation who shall have become bound or engaged as surety, and all bonds for the due execution or performance of any contract, obligation, or requirement, or the duties of any office or position, and to account for money received by virtue thereof, and all other bonds of any description, except such as may be required in legal proceedings, not otherwise provided for in this schedule, 50 cents: *Provided*, That where a premium is charged for the execution of such bonds the tax shall be paid at the rate of one per centum on each dollar or fractional part thereof of the premium charged: *Provided further*, That policies of reinsurance shall be exempt from the tax imposed by this subdivision.

3. Capital stock, issue: On each original issue, whether on organization or reorganization, of certificates of stock by any association, company, or corporation, on each \$100 of face value or fraction thereof, 5 cents: *Provided*, That where capital stock is issued without face value, the tax shall be 5 cents per share, un-

less the actual value is in excess of \$100 per share, in which case the tax shall be 5 cents on each \$100 of actual value or fraction thereof.

The stamps representing the tax imposed by this subdivision shall be attached to the stock books and not to the certificates issued.

4. Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock in any association, company, or corporation, whether made upon or shown by the books of the association, company, or corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock or not, on each \$100 of face value or fraction thereof, 2 cents, and where such shares of stock are without par value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share, unless the actual value thereof is in excess of \$100 per share, in which case the tax shall be 2 cents on each \$100 of actual value or fraction thereof: *Provided*, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of stock certificates as collateral security for money loaned thereon, which stock certificates are not actually sold, nor upon such stock certificates so deposited: *Provided further*, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts: *Provided further*, That in case of sale where the evidence of transfer is shown only by the books of the company the stamp shall be placed upon such books; and where the change of ownership is by transfer of the certificate the stamp shall be placed upon the certificate; and in cases of an agreement to sell or where the transfer is by delivery of the certificate assigned in blank there shall be made and delivered by the seller to the buyer a bill or memorandum of such sale, to which the stamp shall be affixed; and every bill or memorandum of sale or agreement to sell before mentioned shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers. Any person or persons liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person or per-

sons who shall make any such sale, or who shall in pursuance of any such sale deliver any stock or evidence of the sale of any stock or bill or memorandum thereof, as herein required, without having the proper stamps affixed thereto with intent to evade the foregoing provisions shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding \$1,000, or be imprisoned not more than six months, or both, at the discretion of the court.

5. Produce, sales of, on exchange: Upon each sale, agreement of sale, or agreement to sell, including so-called transferred or scratch sales, any products or merchandise at any exchange or board of trade, or other similar place, for future delivery, for each \$100 in value of the merchandise covered by said sale or agreement of sale or agreement to sell, 2 cents, and for each additional \$100 or fractional part thereof in excess of \$100, 2 cents: *Provided*, That on every sale or agreement of sale or agreement to sell as aforesaid there shall be made and delivered by the seller to the buyer a bill, memorandum, agreement, or other evidence of such sale, agreement of sale, or agreement to sell, to which there shall be affixed a lawful stamp or stamps in value equal to the amount of the tax on such sale: *Provided further*, That sellers of commodities described herein, having paid the tax provided by this subdivision, may transfer such contracts to a clearing house corporation or association, and such transfer shall not be deemed to be a sale, or agreement of sale, or an agreement to sell within the provisions of this Act, provided that such transfer shall not vest any beneficial interest in such clearing house association but shall be made for the sole purpose of enabling such clearing house association to adjust and balance the accounts of the members of said clearing house association on their several contracts. And every such bill, memorandum, or other evidence of sale or agreement to sell shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers; and any person or persons liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person or persons, who shall make any such sale or agreement of sale, or agreement to sell, or who shall, in pursuance of any such sale, agreement of sale, or agreement to sell, deliver any such products or merchandise without a bill, memorandum, or other evidence thereof as herein required, or who shall deliver such bill, memorandum, or other evidence of sale, or agreement to sell, without having the

proper stamps affixed thereto, with intent to evade the foregoing provisions, shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding \$1,000, or be imprisoned not more than six months, or both, at the discretion of the court.

That no bill, memorandum, agreement, or other evidence of such sale, or agreement of sale, or agreement to sell, in case of cash sales of products or merchandise for immediate or prompt delivery which in good faith are actually intended to be delivered shall be subject to this tax.

6. Drafts or checks payable otherwise than at sight or on demand, promissory notes, except bank notes issued for circulation, and for each renewal of the same, for a sum not exceeding \$100, 2 cents; and for each additional \$100 or fractional part thereof, 2 cents.

7. Conveyance: Deed, instrument, or writing, whereby any lands, tenements, or other realty sold shall be granted, assigned, transferred or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction, when the consideration or value of the interest or property conveyed, exclusive of the value of any lien or encumbrance remaining thereon at the time of sale, exceeds \$100 and does not exceed \$500, 50 cents; and for each additional \$500 or fractional part thereof 50 cents: *Provided*, That nothing contained in this paragraph shall be so construed as to impose a tax upon any instrument or writing given to secure a debt.

8. Entry of any goods, wares, or merchandise at any customhouse, either for consumption or warehousing, not exceeding \$100 in value, 25 cents; exceeding \$100 and not exceeding \$500 in value, 50 cents; exceeding \$500 in value, \$1.

9. Entry for the withdrawal of any goods or merchandise from customs bonded warehouse, 50 cents.

10. Passage ticket, one way or round trip, for each passenger, sold or issued in the United States for passage by any vessel to a port or place not in the United States, Canada, or Mexico, if costing not exceeding \$30, \$1; costing more than \$30 and not exceeding \$60, \$3; costing more than \$60, \$5: *Provided*, That such passage tickets, costing \$10 or less, shall be exempt from taxation.

11. Proxy for voting at any election for officers, or meeting for the transaction of business, of any incorporated company or asso-

ciation, except religious, educational, charitable, fraternal, or literary societies, or public cemeteries, 10 cents.

12. Power of attorney granting authority to do or perform some act for or in behalf of the grantor, which authority is not otherwise vested in the grantee, 25 cents: *Provided*, That no stamps shall be required upon any papers necessary to be used for the collection of claims from the United States or from any State for pensions, back pay, bounty, or for property lost in the military or naval service or upon powers of attorney required in bankruptcy cases.

13. Playing cards: Upon every pack of playing cards containing not more than fifty-four cards, manufactured or imported, and sold, or removed for consumption or sale, after the passage of this Act, a tax of 5 cents per pack in addition to the tax imposed under existing law.

14. Parcel-post packages: Upon every parcel or package transported from one point in the United States to another by parcel post on which the postage amounts to 25 cents or more, a tax of 1 cent for each 25 cents or fractional part thereof charged for such transportation, to be paid by the consignor.

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